



Corporate Governance and Scams: Lessons to be Learnt

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1. Introduction

All the corporate of the world irrespective of their size are vulnerable to the frauds and scandals related to accounting in the corporate. The various types of scams and frauds in the world have resulted in reducing the reliability of the resources used by the investors while investing. This has in other way made efficiency, liquidity and safety of capital and debt markets susceptible. The accounting fraud has been one of the important reasons behind the fall of corporate such as Enron and Satyam. The most financially affected fraud is the Enron and Satyam which is called as Enron of India, being affected by the accounting and auditing profession. Satyam scam has affected the corporate governance norms prevailing in India and along with the scam it brought to the ground the shares of the software companies. Satyam is till now the greatest scam of India also called as the “Enron of India”. The frauds in US such as Enron led to the passing of Sarbanes-Oxley Act in July 2002, in US and Companies Act, 2013 in India because of Satyam scam which led to addition of new aspect to the corporate governance norms in India. These scams resulted in the increase in focus towards the types of frauds which could be done through accounting. This resulted in imposing the responsibility over the external auditor in performing the audit and providing assurance to the investors that the audit done by them is authentic and independent.

The focus will be on examining and analyzing the Enron scam, how the scam occurred through sequence of the events leading to the scam, the impact of the scam into enactment of Sarbanes Oxley Act. The Satyam scam in India however brought the corporate governance issues at Indian perspective. The impact of Satyam scam resulted into bringing reforms such as Companies Act, 2013. Importances of ethics in corporate sector are being brought into light by these scams.

2. Enron: The Corporate Governance Scam

In 1985 the merger of Inter North and Houston Natural Gas, which were the natural gas pipeline companies, resulted into Enron the first nationwide natural gas pipeline network. The ex-CEO, i.e. Kenneth Lay, of Houston Natural Gas was appointed as Chairman and CEO of the company.¹ In the early 1980s there was a regulatory pattern governing the contracts between natural gas producers which were long term contracts involving less risk but with the deregulation in mid 1980s there was change in regulatory pattern resulting into spot market contract which were short term which were mainly for thirty days. These short term contracts resulted into instability in the market with initial decrease in prices and then subsequent increase in prices.² The Enron took advantage of this deregulation and then it became market maker by buying and selling the standard amount of gas.³ With time their expertise increased and they offered long term contracts and charged a premium over spot prices. In this manner by early 1990s Enron became one of the largest gas trader in North America.

3. Events Resulting into Bankruptcy of Enron

1. From Energy to Natural Gas Trading

Huge debts were incurred by Enron during the process of merger being carried on and for the company’s survival its executives came up with innovative business and diversified strategies to generate cash flow. Because of deregulation in the natural gas sector it was risky to sell and fund natural gas and because of this the banks were unwilling to provide loans especially to the small companies. In 1989 Jeffrey Skilling joined Enron and he projected a way out to the Enron’s credit which required the creation of Gas Bank program through which cluster of suppliers would be able to sell gas to Enron and Enron would be able to sell gas to the cluster of consumers.⁴ Enron charged fees for the transaction and undertook the associated risk. With market power in hand Enron was able to predict future prices accurately which in turn guaranteed the supply and prices. Enron entered in long term contracts with producers so that it can reduce the price fluctuations and it also used forward and future contracts. The gas

¹ Scott A. Wasserman, *Enron on our minds*, BUSINESS LAW TODAY, August 6, 2003, at 39.

² Gerth, Jeff, Richard A. Oppel, Jr., *Regulators struggle with a marketplace created by Enron*, THE NEW YORK TIMES, June1, 2003, at 7.

³ Robert Bryce, *Pipe Dreams: Greed, Ego, and the Death of Enron*, NEW YORK: PUBLIC AFFAIRS, 2002, at 394.

⁴ Tufano, P. and S. Bhatnagar, *Enron Gas Services*, HARVARD BUSINESS PRESS, 109-175 (1994).



banks which was created was later on used in electric energy, futures contracts in paper, coal, water, steel and weather. Enron also started using Special Purpose Entities, so that it can finance many of its transactions.

2. *Mark to Market Accounting System*

The Enron used Mark to market accounting system which can be referred to recording trading contracts value and long-term gas delivery on the balance sheet at the market value.⁵ The Board of Enron along with the SEC gave an approval to this Mark to Market accounting system for gas contracts. In long term contracts this method requires estimation of future incomes, where profits are immediately reported. The important reason behind it is that the actual contracts firmly decide the profitability while it is secondary to fulfill the contract.⁶ Since the future net cash value was the basis of the estimation so it was difficult to predict. The income of Enron also included the estimated income even though it was not received and also there was chance that the future contract could yield additional income or incur loss. Prediction here were optimistic and Enron through this accounting system became generator of huge earning. The mark to market accounting system was used for overstated profits and Enron was able to conceal the losses related to wrong forecast. They were using their gas banks so as to provide loan to the gas producers and in order to record the estimated income they were using the accounting system. There was no profit at present and it could only be generated when at future date gas was delivered. Hence, this way investors were given misleading information due to the high chance of deviation in the estimations.⁷

3. *International Expansion*

The Enron International, Enron's wholly owned subsidiary which carries out international projects like manufacturing and managing of energy facilities remote United States. Subsequently, Enron expended to several other areas like developing power plants and pipelines. Also in 1999, Enron Online (EOL) was created which was successful as in online commodity trade it was handling \$335 billion in 2000.⁸

4. *Complex Form of SPEs and Related Parties*

Enron's expansion required large initial capital investments. Enron's credit rating would be affected and it could not further raise any debt from the market because it had already raised massive debts from the market. Further it was not able to achieve the estimated profit which it forecasted to the investors, as a result in order to manage the fund and risk related to specific assets it entered into partnership and made Special Purpose Entity (or SPE) under the recommendations of Andrew Fastow.⁹ In exchange of interest from SPEs Enron was contributing assets and debts and so as to purchase these assets SPEs were borrowing large sum without debts on books of the company from the financial institutions.

In order to find out that whether a SPE is an entity different from the sponsor there are various rules for the reporting purpose. According to Generally Accepted Accounting Principles (GAAP) following conditions must be satisfied-

- The assets which are sold to SPE must be secluded from transferor of the assets
- The investment made by the third party (independent) should be minimum 3% of the total capitalization of SPE and also that third party must in order to avoid the consolidation be exercising control over the SPE.¹⁰

If the above rules are not fulfilled the SPE will be consolidated with business of the firm which is sponsoring and if the rules are properly followed then the isolation of the sponsor from SPE and the control of independent third party over the SPE then the risk of credit will be reduced. The investors of SPEs used to receive the revenue generated out of the sale of the gas reserves which was acquired by the Enron using the funds from SPEs. Enron by passing the assets to SPEs was able to remove the losses from its books. Enron ensured the investors that in order to compensate them for the risk additional shares would be issued by it but, later on the Enron incurred obligation to issue its own stock because the value of assets fell down.¹¹

Enron had hundreds of SPEs till 2001 and the SPEs were controlled by Enron's executives. Later Enron revealed that they violated accounting standards, according to which it was required independent equity investors should own minimum 3% of assets. Also the investor was required to be outsider and take the responsibility of the risk involved in order to fulfil the condition of being independent. This was major drawback of the scheme of Enron because here the third party was not independent and

⁵ Paul M. Healy and Krishna G. Palepu, *The Fall of Enron*, JOURNAL OF ECONOMIC PERSPECTIVES 17, 3-26 (2003).

⁶ *Id.*

⁷ *Supra* note 5

⁸ Salter, Mal, Lynne Levesque and Maria Ciampa, *The Rise and Fall of Enron*, HARVARD BUSINESS SCHOOL, 903-032 (2002)

⁹ Mimi Swartz with Sherron Watkins, *Power Failure: The Inside Story of the Collapse of Enron*, NEW YORK: DOUBLEDAY A DIVISION OF RANDOM HOUSE, 386 (2003)

¹⁰ *Supra* note 5

¹¹ Gary Giroux, *What Went Wrong? Accounting Fraud and Lessons from the Recent Scandals*, SOCIAL RESEARCH, 75, 1205-1238 (2008).



because of not fulfilling this requirement it was able to not unite the SPEs which was accommodating Enron to decrease its loss and enhance the profit and removing the debts from its account books so that its credibility in the market is enhanced.¹²

Along with the accounting failures the company was also doing mere nominal disclosure with respect to its relation with SPEs. Also the company made the investors to believe that it was protecting the risks involved by making investment in the SPE. But the investors were unaware of the fact that the SPEs were using Enron's own stock as guarantees against the hedges. As a result Enron was never protected from downside risk. Also the chief financial officer Andrew Fastow, who served as SPEs principals, received handsome amount as compensation and returns and violating the fiduciary responsibility towards the Enron's stockholders. Also the other expended business of Enron were not successful and loaded with loss and taxes. Later the risky deals in underperforming investments were unraveled and thus Enron suffered massive cash shortfall.¹³ Dynegy Inc, one of the rival companies of Enron wanted to acquire Enron offering it \$9 billion which would have been moderate premium for the shareholders of Enron but it later on because of the reason that Enron was not completely disclosing the debts on its off-balance-sheet it rescinded and this in turn downgraded the status of Enron to a junk because of which under Chapter 11 Enron went to file for the bankruptcy protection on December 2001.¹⁴

4. Analysis of Governance Failures at Enron

1. Conflict of Interest

To supervise the management of the company is one of the indispensable functions of the Board of Directors so that the interest of the shareholders could be protected by the board. But the Board of Enron relinquished the rules of conflict of interest and allowed Andrew Fastow that he can create SPE's where he along with being the CFO of Enron was also equity holder of the entity. The debts and losses having significant impact over the reported profit of Enron were successfully concealed by SPEs. The Code of Ethics and Business Affairs of the Enron prohibited conflict of interest transactions and would allow such transaction only with the approval of Chairman and CEO taking into account the transactions does not affect the interest of the company.¹⁵

The disclosure of the participation of Mr. Kopper in the Chewco Transaction or the approval of the same by Kenneth Lay or Board of Directors could not be proved by any evidence according the Power Reports. In the Chewco Trnsaction, Mr. Kopper was involved both as the general manager of the company and investor which was in turn violating the Code of Ethics and Business Practices of Enron. The Board of Enron was required to be able to identify such conflict of interest so that it could have been avoided.¹⁶

Furthermore in LJM transaction, again a related party transaction and involved conflict of interest but differed from Chewco in one respect *i.e* this transaction was disclosed and approved by the Chairman and thus the Board approved and ratified the transaction on the account that the partnerships are controlled and are implemented by management. Thus through these partnerships Kopper and Fastow broke their fiduciary duty they owed towards the shareholders and thus again we see there is a breakdown of corporate governance mechanism.¹⁷

2. Board's Failures in Supervision and Lack of Checks And Balances

The breakdown in governance and lack of Board's oversight is evident from the approval of transactions involving conflict of interest. The board of directors of the Enron failed in monitoring and ensuring that the policies and procedure have been complied with in the partnerships. The board of the Enron had the duty to monitor the management in which it failed as the board was told by the management it monitored the transaction but in fact it did not and the board of Enron here failed.¹⁸

The board by giving the duty to **Audit and Compliance Committee** was trying to maintain a system of checks and balance so that the Enron's interest be ensured and protected. The transactions were to be annually reviewed by the committee so as to maintain checks and balances and this was given as the responsibility to the committee by the board. But the control system here was not accurate in controlling; also its implementation was not accurate enough in controlling the transactions and maintaining checks and balances. The related party transaction conducted by the Enron was required to be closely examined and in this committee failed.

¹² Bethany McLean and Peter Elkind, *The Smartest Guys in the Room: The Amazing Rise and Scandalous Fall of Enron*, NEW YORK: PENGUIN (2003).

¹³ *Id.*

¹⁴ *Supra* note 5

¹⁵ Brian Cruver, *Anatomy of Greed: Unshredded Truth from an Enron Insider*, NY: CARROLL & GRAF PUBLISHERS, 2002, at. 384.

¹⁶ Powers, W.R.Troubh and H.Winokur, *Report on Investigation by the Special Investigative Committee of the Board of Directors of Enron Corp*, ENRON CORPORATION, HOUSTON, 2002.

¹⁷ *Supra* note 12

¹⁸ Peter Grosvenor Munzig, *Enron and the Economics of Corporate Governance*, DEPARTMENT OF ECONOMICS STANFORD UNIVERSITY, June 2003.



The **Finance Committee** was shaded with the responsibility of examining and monitoring the transactions. They are supposed to approve, review the transactions and guide the financial policy of the company and the decisions of the company. The related party transactions prima facie shows the failure of the finance committee to monitor the complex transaction and oversee risk.

The **Compensation Committee** was given with the responsibility to supervise the policies of the Enron with respect to compensation to directors, officers and employees but the committee failed in monitoring these policies. If the committee would have reviewed the compensation policies then the excessive compensation given to Fastow and Kooper for management done by them and their private return investments would not have concealed and instead would have been revealed to the public. Thus one of the main reasons behind the financial Enron's failure was because of the lack of oversight by the compensation committee.¹⁹

3. The Responsibility and Accountability Of CEO

The CEO of the company Ken Lay failed in performing his duty of managing the ethical and the legal risks involved in the management of the firm. The company without even considering the ethical scope of making a decision and what can be the possibility of the high risk financial instrument over the stakeholders of the company and they adopted the most complicated models of trade and also the risky transactions. These methods resulted into increasing the importance of ethics. But the CEO of Enron did not find out any of the misconduct going on in the company and dealings with engaged individuals. Also the CEO, even after knowing the fact that Enron was not in good position, in public made the claim that the Enron was working well and there was no problem. Also the internal report shows that he was aware of the misconduct going on in Enron. The ethical norms of the company and the compliance of these norms begins at the top level of the firm where it is the duty of the top managerial persons along with the board of directors that the ethical norms are developed and are complied by so that to eliminate misconduct disasters.²⁰ Now it is the responsibility of Board and CEO that such a business model be adopted which is transparent and also maintain a balance between the risks and the market opportunity. The probability of the ethical risks increases with the managers of lower level being given permission creating profit by making use of loopholes of the regulation. The CEO of Enron if had told the truth to the employees of Enron and public then Enron would have survived.

4. Auditing Issues

Materials on record show that the Audit and Compliance Committee were briefed by Arthur Andersen Auditors about Enron's high risk accounting practices and thus they had knowledge about the accounting methods used in the company but they did not take any action upon them. It was the duty of the committee to see that the financial statements are fair and in conformity with GAAP. They would have diligent enough to question the accounting techniques incorporated in Enron. Even if questions by the Committee were asked from Andersen about the current accounting standards, their expression was one of comfort. The committee was under the duty to produce actual financial statements but because of wrongful sanction given by Anderson of the risky transactions, the committee failed to produce the actual financial statements.²¹

Enron's demise was a result of poor decisions by the Audit and Compliance Committee, management and Andersen auditors. The management should have scrutinized such risky deals involving known conflict of interest. Then Andersen's erred in approving such risky transactions under the SPE's and as a result the Audit and Compliance Committee failed to produce accurate financial statements. Also, the disclosure documents of Enron only in the footnotes of the documents gave the description of these SPEs were given only to the outside investors. It was difficult for the analyst and investors to understand such transactions as according to the non consolidation rules it was not required to include these SPEs in balance sheet. Here the committee would have had open and sincere discussion with management and external consultants of the company.²² Due to the lack of accurate financial reporting the shareholders were deceived as they relied on the information and financial reports produced by management. It was a breakdown of corporate governance mechanism to protect investors.

5. Lack of Auditing Independence

The auditing firm of the Enron was Arthur Andersen, one of the leading accounting firms. Arthur Andersen's main work was to ensure accounts of Enron and that whether they are fair or not giving true reflection of the company's work. The Arthur Andersen was providing along with auditing facilities the external consulting services to Enron which was resulting into conflict of interest of the auditing firm as the auditing firm was receiving was hefty amount from Enron for auditing as well as consultancy. This resulted into compromising their auditing independence in finding out what was the auditing procedure carried

¹⁹ *Id.*

²⁰ Ken Lay, O. C. Ferrell and Linda Ferrell, *The Responsibility and Accountability of CEOs: The Last Interview with Ken Lay*, JOURNAL OF BUSINESS ETHICS, 100, 209-219 (2011).

²¹ *Supra* note 18

²² Emshwiller, John R. and Rebecca Smith. *Corporate Veil—Behind Enron's Fall, A Culture of Operating Outside Public's View*, WALL STREET JOURNAL, December 5, 2001.



on by Enron. As a result Enron's management failed to procure the revised financial statements. Also here we see oversight of Enron's Board broke down. Now the burden is upon Audit and Compliance Committee to find out whether the auditors are independent or not. The committee failed to find out that the auditing services provided by Enron were independent or not. If the Anderson's auditors had only concentrated in their auditing responsibility and not on other services and the firm had been interrogative enough they would have been able to maintain the independent character of the firm. This would have yield accurate financial statements. Thus they failed in their oversight duty which again shows a breakdown of corporate governance in Enron.

6. Director's Independence

Director's independence is indispensable for evaluating their ability in providing objective judgment. According to the *Business Roundtable* (2002), the panel of directors should possess significant level of autonomy from management.²³

It is important to note here that Board of Enron had one executive director. Also the financial relations between the Enron and the directors of Enron were the main reason behind the failure to notice the flaws of Enron. The report of the U.S. Senate Subcommittee on *The Role of Enron's Board of Directors in Enron's Collapse* shows that there were financial ties amongst Enron Board members.²⁴

Prima facie it shows that the Board members were not critical of Enron's management and hence failed on their oversight duty and contributed to Enron's demise. The failure of the board was because of the lack of independence on Board of Enron, this suggests that the Enron had broken another one of the important and elemental corporate governance institutions.

5. Post-Enron Governance Reforms

Sarbanes- Oxley Act of 2002

The Enron scam resulted into enactment of the Sarbanes-Oxley Act, 2002 in America. The main aim behind the enactment of the Act was that the confidence of the investor be restored in the capital market and the frauds in the public companies in the financial statements be eradicated and along with that the penalties being imposed for the frauds be increased so that the frauds becomes less in future.²⁵ Along with that the most important change cam into being with the enactment of the Act was that:

- Creating a Public Accounting Oversight Board.
- For certifying the SEC filings certain requirements are to be fulfilled by the senior financial officers. The financial report should show the true position of the company.
- Personal loans to executive officers are banned.
- The Act prohibits insider trading.
- For financial reporting, all the material off balance sheet transaction is to be disclosed.
- The report is to be conditioned by the code of ethics for senior financial managers and if there are any further changes to be brought into the code of ethics these are required to be disclosed in the report.
- The audit committee and the compensation committee should consist of independent directors to give independent decisions.
- According the Act the most important change brought into is that the external auditors should not be providing services other than auditing services to the company as it may jeopardise the independence of the auditors.
- Along with the above condition the auditing firm shall be not allowed to serve as an auditor to the company for one year if the CEO, CFO or chief accounting officer of the firms conducting the audit of the company has in any of the manner, in any capacity has been participating in the audit of the company at the same time being employee of the auditing firm.
- The auditing company and the reviewing company at the span of five years should be changed.
- According to the Act an Accounting Oversight Board should be established and this board shall be overseeing the firms those are performing the audit of the public company, the board shall also be able to establish rules for governing and regulating the audits, conducting investigations and imposing sanctions.
- Criminal penalties are imposed for securities violations. CEOs and CFOs of the company shall be fined with the \$5 million if they make false statements with respect to the disclosure requirements, or the imprisonment of 20 years, or both.
- New provisions for corporate whistleblowers.²⁶

²³ *Supra* note 18

²⁴ *Supra* note 18

²⁵ Deakin, Simon; Suzanne J. Konzelmann, *Learning from Enron*, ESRC CENTRE FOR BUSINESS RESEARCH, September 2003.

²⁶ Chhaochharia, Vidhi; Yaniv Grinstein, *Corporate Governance and Firm Value: the Impact of the 2002 Governance Rules*, JOHNSON SCHOOL RESEARCH, March 2007.



6. Indian Perspective (Satyam Scam and Post-Satyam Governance Reforms)

Satyam Scam

Satyam was leading Indian IT company at its times before the scam was revealed. The scam was revealed when the board of Satyam has for the acquisition of Maytas Infra Ltd. and Maytas Properties Limited passed the resolution where the Raju's family was having 36% stake in both the companies. This acquisition was questioned by the investors of Satyam to which Raju gave the justification that it was in the best interest of the shareholders but shareholders did not agree with it and started dumping the shares of the company which in result drastically decreased the stock price of the company and there was visible failure of credibility. On 7th January 2009, Raju wrote a letter, confessing that systematically over the past few years the books of the company were cooked and in reality there were only fictitious revenues shown in the books along with inflated cash balances.²⁷ Raju confessed that the Maytas deal was his last attempt to fill the fabricated assets with real one. It was a week after Raju's confession, the auditor of Satyam i.e. Price Waterhouse disclosed that its audit report was based on wrong financial statements provided by the management of Satyam and hence the audit report was wrong. The Satyam announced the acquisition of Maytas without the approval from the shareholders of the company, where Ramalinga Raju took this decision without the approval was only having 8.5% stake in the Company. This acquired company was a company where 36% of the stake with Raju and sons which in result developed interest into this company and this was in knowledge of the board. The board of Stayam was not having a person who can be said to be a financial expert. Though the position of CEO and Chairman were distinguished but the positions were hold by the brothers which can be said to have major in the company and were also holding the high position in the management. Also the non-management directors were meeting only in the presence of management directors.

The scam was portrayed as a deviation so as to rescue the confidence in Indian capital market still some of the commentators have claimed that it was a sign of governance issues in India. Satyam grossly violated all rules of corporate governance.²⁸ It had failed to show good relation with the shareholders and employees. The governance issue in this scam was because of the company not fulfilling their obligation towards stakeholders, the external auditors' reliability.

Governance Issues Involved in the Scam

- 1. Role of Management, Auditor, Bank and Others in Satyam Scandal-** The role of directors is to act in a manner which is for the best interest of company and not in a manner causing conflict of interest of their own and company. In case of any of the conflict they are required to disclose the conflict to shareholders and get their approval in general meeting. This was not done by the board of Satyam at the same time the auditors corroborated in the fraud by considering the documents given by Satyam as authentic.
- 2. Managing Director, CFO and Bank's Role-** According the records of the NSE Mr. Raju along with existing CFO V. Srinivas, A.S Murthy, V. Murli etc sold shares of 3,6500, 3,14,000, 1,83, 000 respectively. These shares were sold even before the scam surfaced so they were sold at really good price. Prima facie it was believed that CFO and Raju were responsible for the fraud but it could not have happened without help of auditors and Banks. As the accounts of the bank were also inflated and showed false account details for extended time. Raju not only inflated the accounts but also the number of people being employed in the company. Through inflated number of employees he made lot of money.
- 3. Independent Director's Role-** The scam also raised the question about the importance of independent directors in the company. According to Companies Act, 1956 strength of independent directors must be at least one third of the board of the company, but these directors are appointed by the company. The board of Satyam had independent directors present but still the scam occurred. As these independent directors were appointed by the promoters of the company who were the main accused of the scam, so the appointment of independent directors was mere disdain. The appointment of independent directors is required because they are supposed to be accountable to the shareholders of the company and their presence plays role in the decision of the board as that would result in a decision which promotes the interest of the shareholders. So the independent directors should be loyal and accountable to the shareholders and not to those who appointed them i.e. the promoters in the present case.
- 4. Auditor's Role-** The scam like Satyam is not possible without corroboration from the auditors i.e. PWC which was the auditor of Satyam when it was charged by CBI for overlooking the irregularities in the accounting system. The auditors of Satyam were primarily held guilty of professional misconduct by ICAI. ICAI constituted a committee to overlook the role played by the auditors of Satyam i.e. PWC in the scam as it certified the accounts of Satyam.²⁹ The Satyam Computer Services' scandal brought to light the importance of ethics and its relevance to corporate culture.

²⁷ Letter dated January 7, 2009 from B. Ramalinga Raju to the Board of Directors, Satyam Computer Services Ltd.

²⁸ Chakrabarti, R., Megginson, W., Yadav & Pradeep K., *Corporate Governance in India*, JOURNAL OF APPLIED CORPORATE FINANCE 20, 1-59 (2008).

²⁹ V. Gopalan, *Corporate Scams in India: Lessons to be learnt*, COMPANY LAW JOURNAL 1, 76 (2009).



Post Satyam Governance Reforms

Even before happening of the scam the Companies Act, 1956 was being updated. The voluntary guidelines were released in the year 2009 for the corporate governance by Ministry of Corporate Affairs. The reform finally resulted into the enactment of Companies Act, 2013 where the liabilities of the directors have been increased to protect the interest of the shareholders. The Satyam Scam resulted into setting up of a CII task force so as to give suggestions in order to avoid scams like it and also the Narayana Murthy Committee was set up addressing the issues related to audit committees, rights of shareholders, and whistle-blower policy.³⁰ Also the SEBI has revised after the scam various requirements of corporate governance and also the financial reporting. The SEBI has also proposed for the protection of the whistle blowers in the company. Other changes brought after the scam are as follows-

1. **Increased Financial Accounting Disclosures-** The SEBI also recently proposed the requirement of disclosing the balance sheets twice a year by the companies. Before the Satyam scam it was required to disclose only once in a year. If there had been increased frequency of disclosure of the balance sheets the Satyam scam would have been prevented as it would have discovered by the investors that something is wrong and the investors would have pressurized the board that investigations be done for the transfer of cash to the accounts which are non-interest bearing accounts.
2. **IFRS (Adoption of International Standards)-** The scam resulted into adopting the international standards for the financial reporting by the year 2011. Adopting these standards will be facilitating the investor to compare the financial performance and hence will be facilitating in increasing the confidence in the accounting numbers.
3. **Independent Directors-** The aftermath of the scam was that the presences of independent directors have been mandated in the company. Earlier the the listed agreement clause 49 with respect to independent directors was only applicable to the listed companies but now the requirement is also applicable for the other companies. These independent directors are now prohibited from receiving any of the remuneration for the services rendered by them other than the reimbursement given to them. Also the independent directors should be there at least one-third of the board and it is mandatory.
4. **Auditors-** Companies Act, 2013 makes the auditor not to perform any services other than auditing services to a company ensuring the independence of the auditing firm and avoiding the conflict of interest. The auditors have been imposed with the duty to report any of the fraudulent act if noticed by them while they are performing their duties. The audit committee of the company is also required to have mandatorily independent directors in majority.

Along with the above mandatory norms various other regulations have been added such as now, it is mandatory to disclose the evaluation of the performance of the BoD, filing of returns with the Registrar of Companies. The stakeholders can now initiate an action against the company and against the auditors for the damages incurred to them which was earlier not available to the stakeholders. What we learned from Satyam was that all the inaccuracies of the firm should be investigated and the strict laws are required to detect any of the inaccuracy in the accounts.

7. Suggestions

After analyzing various issues it is required that following measures should be taken for effective corporate governance -

- **No concentration of Power-** There should not be any concentration as the post of CEO and Chairman should be held by different persons. If the positions are held by the same person then there would be concentration of power and also the person would be lacking in expertise required for a particular position. If both positions are held by different persons there will be checks and balance exercised and if by same person there will be no check and balance.
- **Board's accountability-** It is required that the company's board should be able to give a strategic guidance and leadership to the company; also they should be giving independent judgments and should be in a position to exercise control over the company. It is also required that while exercising the control the board of the company should also be accountable to the shareholders of the company.
- **Independent auditors-** The auditing firms should be qualified enough and also independent to so that it could reveal the financial information of a company while watching over the financial reporting process of that company. the external auditors of the company are required to be independent and should not have interest in the company which they are auditing because if the auditing firm develops a conflicting interest its auditing would be affected by it. They should not be receiving any pecuniary advantages other than compensation from the company for the audit being done.
- **Independence of board-** The board play major role in the running of a company and its development and the same board becomes responsible for the down fall of the company if not performing its responsibilities in the proper manner. Such as board even if aware of the fraud ongoing in the company keeps mum leads to downfall of the company, the board should be accountable to the shareholders and be independent and for that it is required that there should be independent

³⁰ Nasscom, Corporate Governane and Ethics Report, 2010.



directors present in the board in sufficient number and those independent directors should be genuine independent directors.

- **Whistle blower policy-** It required to encourage whistle blower policy and protect the whistle blowers in corporate sector so that if there is any information with respect to fraud going on in the company they can reveal the fraud without any fear. For this the provisions are there in Sarbanes Oxley Act of USA and in India assistance can be taken from these laws.

8. Conclusion

The increase in corporate frauds and need for transparency has resulted into need of forensic skill to unravel accounting exercises resulting into unclear financial statements and also the need of the change in regulatory action has resulted into changing the governance norms across the world. The lack of communication has increased the demand of professional to identify such frauds ongoing in the company. For that it is also needed that the governance norms are strict and are implemented properly. The scams like Enron and Satyam had greater influence over accounting and auditing professions as both the frauds were being corroborated by the auditing firms. Frauds like them resulted into the enactment of Sarbanes-Oxley Act, 2002. The frauds increased the awareness towards frauds and also increased the responsibility of the external auditors in performing the audit and assuring that the financial statements do not have any frauds.

The Satyam scam in India highlighted the importance of corporate governance norms and security laws in Indian markets. It was required that the emerging Indian market should have an environment which promote the corporate governance norms. The Satyam scam has brought into light the importance of corporate governance norms and ethics in the corporate sector of a country. All the kinds of scams have resulted into raising the need and requirement of good conduct which is based on ethics. Like Enron Satyam forced the Indian Government to again frame the corporate governance norms and make strict rules for the auditors. These scams make the government to introduce the norms which are strict in nature and are also implemented properly so that in future the scams do not occur using the same basis of failure.