

WHITE PAPER ON STRENGTHENING ETHICAL CORPORATE GOVERNANCE



Network India

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Executive Summary

“Fighting corruption is part of the fabric of the Department of Justice” said David O’Neil, Acting Assistant Attorney General, Department of Justice’s Criminal Division, U.S. The statement comes in reference to a case of 2006, involving six foreign nationals; participating in an alleged international racketeering conspiracy involving bribes of at least \$ 18.5 million to State and Central Government officials in India to secure licenses for the mining of titanium minerals in the eastern coastal Indian state of Andhra Pradesh. Six defendants charged in the case includes a Ukrainian businessman; a Ukraine national; a Hungarian businessman; an Indian national and permanent resident of United States; a Sri Lanka national and a member of Parliament in India, who was an official of the Andhra Pradesh State Govt. Five of six defendants¹ are also charged with conspiracy to violate the Foreign Corrupt Practices Act (FCPA), among other offenses in June, 2013. This case is indicative of the global aggressiveness of investigation.

In the recently published Ease of Doing Business Index (2015) constituted by the World Bank, India ranked 142 amongst 189 nations in the world (the lower bottom) eight notches down from the ranking of 134 in 2014, indicating that India is an investment/business averse country².

In terms of Ease of Starting a Business, World Bank ranks India at 179, the ranking of countries being based on parameters of business environment, dealing with construction permits, getting electricity, registering property, getting credit, protecting investors, paying taxes, trading across borders, enforcing contracts and resolving insolvency. Lack of transparency and accountability shrouds all the above procedures, as demonstrated through the following table.

The need of ethical corporate governance, in recent times then, is more acute than ever. The White Paper on ‘**Strengthening Ethical Corporate Governance**’ presents the International frameworks & Indian policy regime on Corporate Governance, Challenges of ethical business conduct in India and Focused Recommendations. The paper incorporates feedback and recommendations of stakeholders emerging out of Focus Group Discussions (FGDs) and meetings/consultations conducted by Global Compact Network India under the UK Prosperity Fund supported Project titled ‘Strengthen Ethical and Transparent Corporate Governance Practices and Further Responsible Development’.

Criteria	Ranking
Starting a Business	158
Dealing with Construction Permits	184
Getting Electricity	137
Registering Property	121
Enforcing Contracts	186
Trading across Borders	126
Paying Taxes	156
Resolving Insolvency	137

¹Six Defendants indicated in Alleged Conspiracy to Bribe Government in India to mine Titanium Minerals". Department of Justice, Office of Public Affairs. 14 April 2014.

<<http://www.justice.gov/opa/pr/six-defendants-indicted-alleged-conspiracy-bribe-government-officials-india-mine-titanium>>

²<http://www.doingbusiness.org/rankings>

Introduction

Global Compact Network India has been instrumental in bringing all stakeholders on a common platform through its flagship 'Collective Action Project' and subsequently through 'Strengthen Ethical and Transparent Corporate Governance Practices and Further Responsible Development' Project to promote the 10th UNGC principle which states that "Businesses should work against all forms of corruption including extortion and bribery."

The learning that GCNI had while implementing activities under these projects is that 'one size fits all' approach would not work in the country as diverse, challenging, yet full of opportunities and market potential such as India. The solution lies in providing a neutral platform of learning and knowledge exchange to these stakeholders and thus improving upon individual stakeholder practices apart from providing collective recommendations to the policymakers that emerge from various deliberations. "Furthering Responsible Development" is not an agenda of an individual or a particular stakeholder organisation rather all individuals and organisations have to work in perfect synergy so as to have a desired measurable impact.

This White Paper aims to facilitate discussion to effectively coordinate and liaise with Government representatives, Policymakers, Corporate and Business Federations for effective policy changes in the country on the issue of ethical business conduct and corporate governance practices.



International Transparency Instruments Implemented In India

Since the past two decades the international community has made attempts to introduce regional and global initiatives to curb graft. The idea is to create a platform for collaboration and laying down norms, which could aid in making relevant changes in the legislations of the countries 'party to the initiative'. World Bank and Organisation for Economic Co-operation and Development (OECD) have defined corruption so that uniformity could be established on definition of corruption, while the United Nations and OECD introduced guidelines on International Corporation on corruption. Following are some of the international initiatives/instruments which have been globally acknowledged and are slowly gaining ground and are widely accepted norms of doing business, including India.

Organization of Economic Cooperation and Development (OECD): India ratified OECD's global standard for automatic exchange of information between tax authorities in 2012. This protocol lays down clear information about what kind of information should be shared, leaving no room for comprehension. This includes financial institutions, type/kind of accounts and due diligence procedures to be followed by financial institutions. The aim of this protocol is to combat offshore tax evasion.

United Nations Convention against Corruption (UNCAC): UNCAC is one of the most comprehensive documents to tackle corruption, specifically talking about public and private bribery, including active and passive acts. It mandates for a whistle blower protection mechanism. Further, UNCAC has an "Asset Recovery" clause which elaborates the cases and the extent of asset that could be recovered in an event of company involved in fraud. India ratified UNCAC in May 2011 and since then many legislative changes have been made to address graft.

UK Bribery Act: UK Bribery Act, a comparatively recent instrument, has gained prominence in anti-corruption discussions worldwide. UK Bribery Act does not confine itself to just the bribe taker but extends the penalties to a person/company which makes payment leading to an act of corruption. Experts have called this Act to be one of the toughest till date. The Act makes provisions of punishment for even those companies that do not have adequate mechanism in place to tackle corruption. The jurisdiction of this Act is on UK based companies and their subsidiaries across the globe.

Integrity Pact: Transparency International's Integrity Pact (IP) is another widely accepted instrument to bring about transparency in procurements. Integrity Pact has found a firm ground in India, with forty eight Central Public Sector Undertakings adopting the pact, till February 2015. Efforts are being made to encourage state level public sector undertakings and the private sector to adopt IP.

Foreign Corruption Practices Act (FCPA): FCPA is an instrument which penalizes any act of corruption committed in US or by any US citizen in any part of the world. Additionally, any case of corruption in which the transaction is done in US dollars also comes under the gambit of FCPA. The Act defines corruption as a payment made to any public official, political party and any other individual which would influence a business decision. As FCPA has emerged as an internationally accepted instrument/norm, many companies, irrespective of their operations in the US, have adopted some of the features of FCPA, the most widely adopted clause being the 'Gift Policy'. Several global companies adhere to strict gift policies.



Legislative Changes To Curb Corrupt Practices in India

The public discourse around anti-corruption and business transparency has gained tremendous momentum in the last few years in India, resulting in legislations like the Whistleblower Protection Act, 2011, Companies Act, 2013, Lokpal and Lokayuktas Act, 2013, among others. Many prominent Indian companies have upgraded their internal mechanism vis-a-vis corruption risks and have tried to mitigate the prohibitive costs attached to corruption. Some of the major Indian legislations addressing graft are:

Whistleblowers Protection Act 2011

Overview

Passed in 2014, it establishes a mechanism to register complaints on any allegations of corruption or wilful misuse of power against a public servant. The Act safeguards against victimization of the person who makes the complaint.

Mandate

Complainant: A complainant could be any person making a public disclosure related to an act of corruption, misuse of power or criminal offence by a public servant.

Protection to whistleblowers: To ensure that the complaint is genuine, the identity of the person filing such a complaint is required. The authorities do not divulge the name of the whistle-blower. As a safeguard, heavy penalties are imposed on people who disclose the identity of the whistle-blower.

Area of Future Intervention

- Outsourcing of Grievances Division: To gain confidence of the employees and encourage reporting Grievance Redressal Division should be outsourced.
- Definition of Victimization: The present legislation has not defined what is categorized as victimization. It is proposed that the parameters of what accounts for victimization should be clearly laid down.
- Anonymous reporting of corruption: The provision of anonymous reporting is not present in the Act. Anonymous reporting could encourage people/employees to come forward and report wrongdoings in the organizations without disclosing their identity.
- Protection for Women: It was observed that women, in a number of cases, are the whistle blowers. Provisions should be made in the Act to protect women.

Companies Act 2013

Overview

Passed in 2013, the act consolidates and amends the law relating to companies. New clauses relating to compliance requirements by a private sector have been introduced for the first time in this Act.

Mandate

The Act 2013 is expected to facilitate more business-friendly corporate regulations; improve corporate governance norms, enhance the accountability on the part of corporate and auditors, raise the levels of transparency and protect the interest of investors, particularly small investors.

Area of Future Intervention

- Companies Act 2013 does not include specific punishments and penalties for illegal deposits.
- Reporting of fraud by auditors over and above a threshold limit to the government needs to be mandatory.

Right To Information Act 2005

Overview

The Act provides for setting out the practical regime of Right To Information for citizens to secure access to information under the control of public authorities, in order to promote transparency and accountability in the working of public authority.

Mandate

Public Authority means any authority or body or institution of self government established or constituted by or under the constitution, by or any other law made by the Parliament, by the state legislature, notice issued or order made by the Government etc.

Area of Future Intervention

- Right to Information (Amendment) Bill 2013 has removed the political parties from the definition of public authorities. This particular amendment should be removed from the bill.
- Political funding should be open to public scrutiny.

Lokpal and Lokayukta Act 2013

Overview

Passed in 2013, Lokpal (Ombudsman) for the Union and Lokayukta at the state to examine allegations of corruption.

Mandate

A Lokpal is an ombudsman (legal representative) in India having jurisdiction over all Members of Parliament and central government employees in cases of corruption.

Area of Future Intervention

- The Act provides that a public servant should declare his / her assets within thirty days of assuming office. The details of such declaration should include: (i) liabilities and (ii) assets jointly owned by them, their spouse and dependent children, or assets for which they are beneficiaries.
- Additionally the declaration should include (i) Movable and immovable property owned, inherited, acquired, or held on lease by them or their family; and (ii) debts and liabilities incurred directly or indirectly by them.

Prevention of Corruption (Amendment) Bill 2013

Overview

Prevention of Corruption Act passed in 1988 is an Act to curb corruption amongst public officials. Amendment to Prevention of Corruption Act has been introduced in the Upper House of the Indian Parliament.

Mandate

The definition of 'public servant' includes office bearers of cooperative societies receiving financial aid from the government, employees of universities, Public Service Commission and banks. The Act has clearly defined what will account for bribery and also the associated punishment that would be levied on such public servants indulging its acts of bribery and corruption. Overall, bribe taking is considered as a criminal offence.

The proposed amendment of the act are:-

- The Bill redefines criminal misconduct to cover misappropriation of property and possession of disproportionate assets.
- The Bill modifies the definitions and penalties for offences related to taking a bribe, being a habitual offender and abetting an offence.
- Powers and procedures for the attachment and forfeiture of property of public servants accused of corruption have been introduced in the Bill.

Area of Future Intervention

- The concept of 'active' and 'passive' bribe, absent in any Indian legislation, needs to be brought in.

Prevention of Money Laundering (Amendment) Act 2012

Overview

The Act introduces the concept of 'corresponding law' to link the provisions of Indian law with the laws of foreign countries. It also adds the concept of 'reporting entity', which would include a banking company, financial institution, intermediary or a person carrying on a designated business or profession.

Mandate

The Act expands the definition of offence under money laundering to include activities like concealment, acquisition, possession and use of proceeds of crime.

Area of Future Intervention

- Keeping pace with the international developments, Prevention of Money Laundering Act 2012 should insert clauses on information exchanges, as they are vital towards curbing outflow of 'illegal money'.

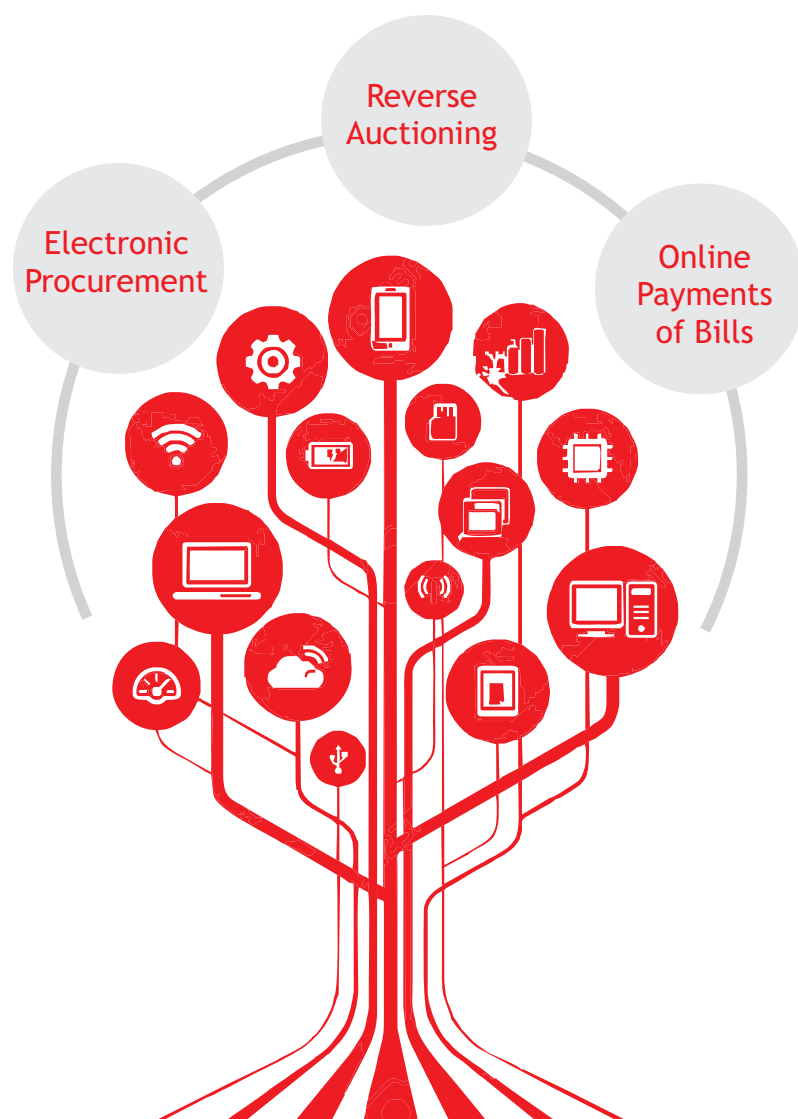


Technological Innovation To Curb Corruption

Technology has proved to be a boom to bring about changes and address some of the complex issues like corruption. With the penetration of mobile and internet there have been several technology led changes and systems which have been put in place to address corruption. For example Janaagraha Centre for Citizenship and Democracy, an NGO has developed the 'I paid a bribe' website (<http://www.ipaidabribe.com/>), which analyses market prices of bribes, based on user reports.

In the state owned businesses facilitation payment has been reduced through the introduction of 'Electronic Procurement' also known as E-Procurement. E-Procurement has been defined as 'Purchasing of goods or services using the internet: e-catalog, e-auction etc'. E-procurement has been fairly successful in curbing facilitation payment.

Several leading public sector undertakings have adopted e-tendering for goods and services contracts. Central Public Procurement Portal has been designed by the government to facilitate all the central government organizations to publish their tender enquiries, corrigendum and award of contract details. The system also enables the users to migrate to total electronic procurement mode. Gradually state governments have started adopting electronic procurement systems. Some of the states which have adopted e-procurement are Rajasthan, Kerala, Tripura and Chhattisgarh.



In GCNI's publication 'Business Case for Anticorruption in India: Principles, Economics and Applications of Transparency Tools' (2015), National Mineral Development Corporation (NMDC) elaborates the merits of electronic tendering. NMDC shares information of a few cases where the use of e-tenders has resulted in greater economy, wherein the difference between quoted and purchase price has led to increase in profit margins by 15%-38%. During the year 2013-14, 18% of the procurement in NMDC was conducted electronically. Also with e-procurement NMDC was able to reach out to wider number of suppliers, who provide better products and services, at best prices and at the same time avoid cartel formation.

■ **Reverse Auctioning** has found its ground with the spurt of technological innovation. Reserve auction is an auction where the item for sale may not be sold if the final bid is not low enough to satisfy the buyer; and then the buyer reserves the right to accept or reject the highest bid. This method of auctioning has been employed by a number of companies where the vendors submit online bids. Mostly service contracts are awarded through reverse auctioning.

In the above GCNI publication KRIBHCO demonstrated, in a step by step manner, its process of procurement of 150 lakh HDPE bags through reverse auction. In addition to a saving of INR 1.99 crores in the entire process, KRIBHCO could achieve the goal of effective, efficient, economic and transparent purchase process and could promote healthy competition amongst its vendors. Through a time bound process KRIBHCO could essentially avoid collusion amongst potential bidders, and ensure a tension free environment during the negotiations.

■ **Bill Watch System (BWS)** was introduced by GAIL, a leading Indian PSU. BWS is a system in which the vendors can submit their bills online, a stipulated period has been given to clear the payment and vendors can check the status of their bills online. This system has reduced the human interface and thus largely curbed facilitation payment.

In GCNI's publication 'Raising the Bar Through Collective Action: Anti-corruption Efforts in Action in India' (2012), GAIL demonstrated how BWS led to the transition from paper based processes to electronic document management which has benefited the vendors and employees tremendously. The use of online forms, workflow, reporting and other tools which are part of BWS enabled GAIL to streamline the bill settlement process and reduce the time from 20 days to less than 7 days.

Challenges To Ethical Business Conduct In India

Significant challenges to ethical business conduct include:

- **Concentration of Ownership and Control** - High ownership concentration and control by dominant shareholders raises the entrenchment problem with disregard for minority shareholders.
- **Enforcement and Sanctions** - Law enforcement and sanctions do not act as sufficient deterrents to promote ethical business conduct. Multiple gatekeepers, low conviction and slow prosecution rate, oversight by the regulators, and delay in the judicial system are challenges for effective enforcement of rule of law.
- **Public Procurement** - Public Procurement is Prone to corruption and fraud due to discretionary powers of public officials leading to favouritism, bid-rigging, false billing, kickbacks.
- **Supply Chain** - Involvement of suppliers, particularly SMEs, pose a significant challenge to ethical business conduct as they may avoid necessary licensing, evade legitimate law enforcement, compromise product quality and be susceptible to kickbacks due to their limited financial and other resources.
- **Bribery and Fraud** - It includes instances of tax evasion, counterfeiting, distorting share markets, falsification of accounts, frauds in the banking system, smuggling, money laundering, insider trading and even bribery.



Findings & Recommendations

GCNI, through its multiple focus group discussions, consultations and conferences, has developed following recommendations for strengthening ethical corporate governance in India.

Policy

- Social Audit and post execution audit should be incorporated in further legislations.
- Development and promotion of ethical corporate governance guidelines should be a board room issue.
- Management as a policy initiative should encourage adoption of e-governance and anti-corruption clause in all contracts.
- Management should also develop clear monitoring policies and guidelines for execution of contracts to ensure all rules and regulations are adopted in the execution phase.
- SEBI is confined to overseeing the functioning of listed companies. Mechanism should be framed so that the rules laid for listed companies for disclosure should be adopted by/applicable to non listed companies.
- Private sector should play an active role in the policy making mechanism, first step would be to disclose credible data of their procurement process




Implementation Changes

- Anti-Corruption mechanism of detection, conviction and punishment should be clearly defined and time bound, so that the complainants are encouraged to report.
- An independent tool should be set up by each organization to check the level of corruption and help gauge the performance of the internal Anti-Corruption mechanism.
- Internal Anti-Corruption initiatives/instruments should be utilized to create brand for an organization. Further, the prime focus should be to address the concerns of the 'stakeholders', in this case it could be the vendors, shareholders, employees and the end users (customers).
- In India, Audit office is limited to State capitals; it was recommended that District level Audit Office should be opened, so that a large number of organizations can come under the audit scanner.
- To tackle facilitation payment, services for quick processing of project files should be established. In the Indian context, "Tatkalsewa" could be looked into.



Subject Based Recommendations

Supply Chain	Procurement	Small and Medium Scale Industries
<ul style="list-style-type: none">■ Businesses should focus on asset utilization, route optimization, shipping unit design, consolidating movements, lower emissions in transit, fleet capacity utilization and multi modal network.■ Water transport should be promoted as efficient and economic means of transport.■ Organized the unorganized road transport system e.g. drivers security, leading to their welfare.■ Public Private Partnership model in coastal shipping should be encouraged.	<ul style="list-style-type: none">■ In case of technical procurement or a new product procurement, special care should be taken to procure such goods from vendors having a proven track record for manufacturing /producing the same specifications.■ Specialized cadre of technical experts on procurement in large procurements work should be developed.■ Companies can adopt Strategic Sourcing Process wherein same company is not selected year after year for the tender or similar kind of project.■ Due to the overlap in General Financial Rules and Central Vigilance Commission rules, the Government should take concrete steps to make the procurement process in India transparent and efficient.	<ul style="list-style-type: none">■ Small and medium enterprises which has been out of the anti-corruption policy dialogue should be included in the debate and capacity building of SMEs should be stressed upon.■ SMEs should have internal mechanism in place to check corruption.■ International organizations should put a greater focus on small and medium enterprises (SMEs) in case of anti-corruption initiatives and tool development.



Anti-Corruption Instrument: Integrity Pact

Some of recommendations put forth for increasing the reach and effectiveness of 'Integrity Pact' are:

- Make IP a System-improvement tool from its present complaint handling orientation
- Entire process from procurement to delivery has to be extensively monitored through IP.
- Pre-qualification criterion is important in the procurement process. It is imperative to have capacity building of bidders even in pre-bid cases along with other stakeholders.
- Institutional Arrangement for regular Vendor Meets for periodic feedback from vendors on effectiveness of IP to bring about continual improvement.
- Efforts should be taken towards awareness and updation on IP related issues among contractors /vendors /suppliers /sub-contractors.
- Engage with Independent External Monitors (IEMs) for Process/System improvements based on their experience in dealing with IP issues.
- Complaints under Integrity Pact should be categorized into two categories- Vigilance angle and Terms & Conditions. CVOs should be concerned with Vigilance angle while IEMs should look into T&C.
- Specific legal obligation should be added to IP to enhance its acceptance ratio in Private sector and its clauses should be amended according to present day needs.



Other Recommendations

Training and Education:

- Training and education on anti-corruption for all the stakeholders, especially suppliers and employees.
- Collaboration and information exchange recommended between supply chain and regulators.

Technology Interventions:

- Adoption of Information and Communication Technology (ICT) to enhance vendor management in companies.
- Adoption of ICT in procurement and bill payment should percolate to all sizes of organisations.
- Enhanced reliance on technology like cloud computing vigilance system and swift grievance redressal mechanism.

Collective Action:

- Stakeholders should act collectively rather than in isolation to address corruption challenges in a holistic manner.
- Need for strengthened institutional mechanism for industry associations like CII, FICCI, ASSOCHAM
- Enhanced collaboration by UN bodies like UNODC and UNGC in promoting ethical and responsible business.
- Need for close corporation from and amongst international organizations such as UNGC, PACI, and TI.



Way Forward

- Adoption of a collaborative approach amongst civil society, business and government essential in improving transparency, ethics and integrity.
- Knowledge sharing of good practices, training material and resources to support the implementation of integrity programs and control procedures, and to raise awareness in both the public and private sectors.
- Development and training of employees and third parties periodically on the compliance requirements and consequences of non-compliance through the prevent, detect and respond approach.
- Broaden the base of certain international instruments such as IP by inclusion of various other sectors e.g Real estate, banking etc.
- Combination of expertise, greater pro-active role, capacity building through certifications, trainings and secretarial support for IEMs (companies adopting IP), Compliance and Vigilance Officers is required along with devising legal frameworks.
- Penalization for noncompliance of anti-corruption norms should be advocated.
- Grievances mechanism and Whistleblower protection measures need to be improved continuously.
- Strengthening Ethical Corporate Governance should follow the process of Prevent, Detect, Respond and Continuous improvement.



ABOUT UN GLOBAL COMPACT

The UN Global Compact is a strategic policy initiative for businesses that are committed to aligning their operations and strategies with ten universally accepted principles in the areas of human rights, labour, environment and anti-corruption. With over 12,000 corporate participants and other stakeholders from over 145 countries, it is the largest voluntary corporate responsibility initiative in the world. Endorsed by chief executives, the Global Compact is a practical framework for the development, implementation, and disclosure of sustainability policies and practices, offering participants a wide spectrum of work-streams, management tools and resources — all designed to help advance sustainable business models and markets. Recognizing that business is a key player in the fight against corruption, the UN Global Compact's 10th Principle calls on participants to integrate anti-corruption policies and measures into their strategies and operations.

ABOUT GLOBAL COMPACT NETWORK INDIA

The Global Compact Network India ranks among the top 3, out of the 102 local networks in the world, and has emerged as the largest corporate citizenship and social responsibility organization in the country with a pan Indian membership. With a membership of 183 corporate participants and organizations, the local India network, in the last 12 years of its functioning, has created a strong niche for itself. GCNI members represent pertinent sectors of the country such as private and public sector enterprises, civil society, and academia; collectively deliberating and developing a common development agenda on sustainable development.

ABOUT STRENGTHEN ETHICAL AND TRANSPARENT CORPORATE GOVERNANCE PROJECT

Global Compact Network India's 'Strengthen Ethical and Transparent Corporate Governance Practices and Further Responsible Development Project' is supported by the UK Prosperity Fund India Programme. The Project is part of a wider goal of mainstreaming Anticorruption Collective Action in the development agenda of India. Indian businesses are already witnessing a rise in ethical and transparent governance practices. This Project further strengthens the trend by bringing together senior stakeholders, in business and bureaucracy, to take forward the collective agenda of transparency and responsible development forward. The Project facilitates constructive dialogue and bridges the gap in knowledge of anticorruption instruments and sector-specific challenges to transparent and sustainable development agenda in India.



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