

Corporate Governance Practices under the Companies Act 2013: Evidence from Indian Listed Companies

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Abstract:

Following the Companies Act 2013, governance reforms introduced in India were a huge regulatory step towards good governance that would make the companies more accountable, transparent and protect investors. We empirically confirm the effectiveness of these reforms by analysing governance compliance among companies listed on the National Stock Exchange of India. And we focus on governance aspects such as board composition, independence of directors, audit committee performance, gender diversity and corporate disclosure. We use a panel dataset of listed firms in the post-reform period and rely on econometric methods to investigate the effects of governance quality on firm performance indicators such as ROA and market valuations. More robust governance mechanisms, specifically independent audit control and diversified boards, are better for the firm in terms of financial performance, information asymmetry reduction and investor confidence. In addition, the outcome of the study also demonstrates that governance reforms under the Companies Act 2013 do more than just compliance and lead to a positive impact in corporate monitoring and financial stability. The study contributes to the emerging market corporate governance literature by offering evidence from a promoter-driven ownership environment and highlights the importance of institutional enforcement in conjunction with legal reforms. Policy implications for regulators in order to enhance governance monitoring and ensure sustainable corporate performance in India's ever-evolving capital market system are offered.

1. Introduction:

1.1 The Regulatory Shift: From Clause 49 to the Companies Act 2013

Corporate governance in India has changed radically in the last two decades from voluntary governance to a statutory framework. The first modern governance regulation was the Listing Agreement (Clause 49) made by the Securities and Exchange Board of India (SEBI) in the early 2000s. Clause 49 was focused on improving disclosure standards, board independence and the empowerment of audit committees in listed companies. Although it was an important step in aligning Indian governance with international standards, its enforcement was primarily based on the stock exchange's compliance laws, not on statutory legal authority.

The Companies Act 2013 was a major shift from a disclosure-based regime to legally enforceable governance accountability. Unlike previous regimes, the Act incorporated corporate governance into company law and thus extended corporate governance not just to the listed entity but to corporate structure and managerial responsibility as well.

Key governance reforms under the Companies Act 2013 include:

- The requirement for independent directors and women directors to be appointed as directors of such boards.
- The establishment of committees for audit, nomination and remuneration, and stakeholder relationship committees.
- Enhanced financial disclosure and transparency requirements.
- Corporate social responsibility (CSR) obligations for directors.
- Strengthened accountability and fiduciary duties for directors.

This transition signalled India's transition from "recommendatory governance standards" to a "rules-based governance ecosystem", and was a result of global corporate scandals and financial crises. And the reform was not just to control corporate behaviour but also to restore investor confidence, protect minority shareholders and improve capital market efficiency.

Problem Statement: From "Form" to "Substance"

Despite the big changes in policy, one question remains: Do stronger governance regulations have any real impact on corporate behaviour, or do some firms simply comply formally without any changes in their own behaviour in corporate culture?

Many scholars argue that corporate governance reforms in emerging economies in particular lead to 'symbolic compliance' (sometimes called "box-ticking governance" by some) with respect to governance. Companies may technically satisfy legal provisions by appointing independent directors or forming committees, but these mechanisms may be ineffective in practice.

In the Indian context, structural challenges complicate substantive governance transformation:

- Concentrated promoter ownership.
- Family-owned business groups.
- Informational asymmetry between management and minority shareholders.
- Cultural emphasis on relationship-based decision-making not institutional oversight.

As such, compliance with governance norms may reflect legal compliance rather than behavioural change. The question is whether governance reforms under the Companies Act 2013 have been successfully carried out beyond the usual procedural frameworks and delivered tangible results in accountability, transparency and corporate performance.

Research Objective: Bridging Legal Mandates and Financial Performance

Our research aims to empirically quantify whether stronger governance standards translate into better firm-level performance for Indian listed companies. In particular, we try to bridge the gap between legal governance and economic performance.

The research objectives are:

1. To assess the extent of corporate governance compliance of firms listed on the NSE following the Companies Act 2013 reforms.
2. To study the influence of board composition, independence, audit oversight, and disclosure practices on the performance of firms on ROA and market valuation.
3. To investigate whether governance reforms increase investor confidence and financial stability as opposed to merely fulfilling regulatory requirements

By connecting governance compliance to observable financial performance, the study contributes to the understanding of whether regulatory reforms act as "effective institutional mechanisms" or remain largely procedural requirements of governance.

In so doing, this research contributes to the larger debate in the corporate governance literature on the effectiveness of regulatory intervention in emerging markets and positions India as an important case study in the transition from governance form to governance substance.

2. Institutional Context & Legal Framework

2.1 The Landmark Changes under the Companies Act 2013

The Companies Act 2013 was one of the most comprehensive corporate governance reforms in India's post-liberalization era. In addition to disclosure-based norms in governance, the Act institutionalized accountability through legally enforceable provisions that govern board independence, stakeholder responsibility and ethical corporate behaviour. Among its many reforms, three provisions fundamentally changed governance structure in Indian companies: Section 135 (Corporate Social Responsibility), Section 149 (Independent Directors), and the Woman Director mandate.

2.2 Section 135: Corporate Social Responsibility (CSR)

Section 135 introduced a globally unique statutory CSR framework, making India the first major economy to mandate corporate social responsibility spending through legislation. Companies meeting specified financial thresholds—based on net worth, turnover, or profitability—are required to:

- Establish a CSR committee of the board.
- Allocate at least 2% of average net profits toward socially beneficial activities.
- Disclose CSR policies, implementation strategies and results in annual reports.

The purpose of this provision goes beyond philanthropy; it is to embed stakeholder capitalism into corporate management. CSR obligations encourage companies to internalize environmental, social and community responsibilities and to align corporate strategy with sustainable development goals.

In terms of governance, Section 135 expands the board's fiduciary responsibility from shareholders only to a larger stakeholder ecosystem and redesigns the accountability paradigm of Indian corporations.

2.3 Section 149: Independent Directors

Section 149 institutionalizes the role of independent directors as a central governance safeguard. It mandates that listed companies maintain a prescribed proportion of independent directors who are free from managerial or promoter influence.

The reform attempts to address longstanding governance concerns by:

- Strengthening oversight over executive management.
- Enhancing monitoring of related-party transactions.
- Protecting minority shareholder interests.
- Improving transparency in financial reporting and risk management.

Independent directors are expected to act as 'professional monitors' reducing opportunistic managerial behaviour and making a balanced decision-making process of boardrooms. The provision aligns Indian governance norms with international standards as laid out by international organisations like the Organisation for Economic Co-operation and Development (OECD).

But the effectiveness of independent directors relies not only on formal appointments but also on actual independence, expertise and willingness to challenge dominant promoter interests—the very subject of empirical governance debates.

2.4 Woman Director Mandate

The Companies Act 2013 also required gender diversity as a requirement that certain classes of companies appoint at least one woman director in their boards. This provision seeks to:

- Promote inclusive leadership and diversity in corporate decision-making.
- Improve governance quality as we look from different perspectives.
- Align Indian companies with global Environmental, Social, and Governance (ESG) expectations.

Gender diversity is increasingly associated with better board deliberation, risk assessment and ethical oversight. The mandate therefore represents not only a social reform but also a governance innovation to make board effectiveness.

2.5 The Indian Corporate Ecosystem: Promoter Dominance and Agency Conflicts

In order to understand the impact of governance reforms, it is important to explore India's unique institutional structure. Unlike dispersed ownership structures common in Anglo-American markets, Indian listed companies are predominantly 'promoter-controlled firms', where founding families or business groups still hold huge power and influence over operations.

This ownership concentration fundamentally alters the classical agency problem that is discussed in corporate governance theory.

Type I Agency Conflict: Manager vs. Shareholder

In widely held companies, the typical agency problem is between professional managers and dispersed shareholders. Governance mechanisms such as independent boards and audit committees are designed to prevent managerial opportunism, excessive executive compensation, and inefficient investment decisions.

While this conflict exists in India as well, it is much less severe as promoters are often directly involved in management and thus ownership is usually a conflict with control.

Type II Agency Conflict: Controlling Shareholder vs. Minority Shareholders

The more significant governance problem in India is the type II agency conflict that arises between controlling promoters and minority shareholders. Possible risks include:

- Related-party transactions favouring promoter entities.
- Expropriation of minority shareholders' wealth.
- Information asymmetry and selective disclosure practices.
- Family control prioritizing over shareholder value maximization.

Regulatory oversight by institutions like the Securities and Exchange Board of India (SEBI) attempts to mitigate these risks and control them through disclosure requirements, board independence rules and more rigorous compliance monitoring.

2.6 Governance Reform within Institutional Reality

The effectiveness of the Companies Act 2013 must therefore be assessed in this promoter-driven ecosystem. Legal mandates like independent directors, CSR committees, and gender diversity aim to establish “institutional counterbalances” against concentrated ownership power. However, governance transformation is a question of whether these mechanisms work substantively—active monitoring, ethical oversight and stakeholder engagement—or only procedural requirements for regulatory compliance. Thus, the institutional framework of India is an important test ground for assessing whether statutory governance reforms can change corporate behaviour in the emerging markets of concentrated ownership and evolving regulatory capabilities.

3. Literature Review & Hypothesis Development

Corporate governance literature has studied the importance of internal governance mechanisms to business performance, transparency and investor confidence in the firms. The Companies Act 2013 strengthened the board structure and monitoring as well as providing an empirical framework to examine whether formal governance changes translate into real-world financial results. In this section, we review the previous theoretical and experimental work and develop testable hypotheses.

3.1 Board composition and Firm value.

Board composition is one of the most important internal governance mechanisms. Agency theory suggests that effective boards will reduce conflicts between management and shareholders by providing monitoring, advisory, and strategic oversight functions.

There are early governance studies that show the value of the independent directors in monitoring and controlling managerial opportunism. Michael C. Jensen and William H. Meckling have shown that separation of ownership and control requires independent oversight.

Empirical evidence generally supports the view that higher board independence improves firm value through:

- Enhanced monitoring of executive decision-making.
- Better disclosure quality.
- Stronger risk management practices.
- Protection of minority shareholder interests.

Board independence is especially important in emerging markets as ownership concentration and promoter dominance can undermine internal accountability. Independent directors are institutional protections against related-party transactions and governance capture.

In recent Indian studies, companies that comply with stronger board independence requirements show higher market valuation and operational efficiency. But critics contend that independence “in form” does not always yield independence “in substance”, especially in cases where social or professional networks influence board functioning.

3.2 Gender Diversity and Board Effectiveness

Women directors under the Companies Act 2013 reflect a growing recognition that board diversity is critical in order to enhance governance outcomes.

Theoretical arguments for gender diversity include:

Deepened cognitive perspectives to decision-making. Greater ethical sensitivity and stakeholder orientation. Less groupthink on board discussions. More focus on compliance and risk oversight.

International evidence shows that gender-diverse boards are associated with higher profitability, better ESG performance, and a better corporate image. For the Indian context, the requirement of a woman director was an experiment that allowed researchers to investigate if diversity is important for financial performance indicators (ROA).

While some authors posit that early appointments were symbolic compliance measures of this kind, recent evidence suggests that institutional learning effects such as diversity build board deliberation quality over time.

3.3 Audit Quality and Information Asymmetry

Information asymmetry between managers and investors remains a fundamental governance challenge. Audit committees are a key part of financial transparency and credibility of corporate disclosures.

With the establishment of independent audit committees we aim to:

- Strengthen financial reporting oversight.
- Reduce earnings manipulation.
- Improve internal control systems.
- Enhance investor confidence.

A signalling theory perspective suggests that good audit committees send positive signals to capital markets regarding governance quality. Independent audit committee members, particularly those with financial expertise, are more likely to challenge aggressive accounting practices.

Prior empirical studies show that firms with independent audit committees have:

- Lower discretionary accruals.
- Reduced earnings management.
- Higher audit quality.
- Greater earnings persistence.

In emerging nations like India, audit committees are even more important due to institutional weaknesses, concentration of ownership, and evolving enforcement mechanisms.

3.4 Hypothesis Development

Based on the theoretical foundations of agency theory and resource dependence theory and governance monitoring mechanisms, the following hypotheses are proposed:

- H₁: Board diversity (Gender) is positively correlated with firm performance measured by Return on Assets (ROA). This hypothesis assumes that gender diversity will enhance board effectiveness through better monitoring, balanced decision-making and strategic thinking and decision-making.
- H₂: Audit committee independence greatly reduces earnings management. Independent audit committees would be able to enhance financial transparency and limit opportunistic accounting practices, thus increasing the quality of reporting.

4. Research Methodology

4.1 Research Design

This study employs a quantitative empirical research approach to understand the relationship between corporate governance practices and firm performance of companies listed in the Indian stock market. To do so, the panel data framework is used to analyze the company's performance on a cross-sectional as well as time-series basis. So the empirical approach can be used to determine whether the change in governance proposed in the Companies Act 2013 leads to tangible financial outcomes rather than just better formal compliance.

Sample selection and data sources are used for this study as the NSE of India is regulated by the National Stock Exchange of India. Non-financial NSE-listed companies: we will sample companies with continuous

listing in the study period as long as annual reports and governance disclosures are available. We do not sample financial institutions, as banking and insurance markets are regulated differently. We are doing this for the study period after the implementation of Companies Act 2013 (e.g., 2014-2023).

Data Sources: we will sample annual corporate reports of companies and corporate governance disclosures.

4.2 Variable Measurement

Dependent Variables

1. **Return on Assets (ROA):**

Measures firm operating performance.

$$ROA = Total\ Assets / Net\ Income$$

2. **Earnings Management (EM):**

Proxied using discretionary accruals estimated through the Modified Jones Model.

Independent Variables

- **Board Gender Diversity (BGD):** Presence or proportion of women directors.
- **Audit Committee Independence (ACI):** Percentage of independent directors in audit committee.

Control Variables

To avoid omitted variable bias, the following controls are included:

- Firm Size (log of total assets)
- Leverage ratio
- Firm age
- Industry effects
- Ownership concentration

Econometric Model Specification

Model 1: Governance and Firm Performance

$$ROA_{it} = \alpha + \beta_1 BGD_{it} + \beta_2 BSIZE_{it} + \beta_3 FSIZE_{it} + \beta_4 LEV_{it} + \epsilon_{it}$$

Model 2: Audit Committee and Earnings Management

$$EM_{it} = \alpha + \beta_1 ACI_{it} + \beta_2 FSIZE_{it} + \beta_3 LEV_{it} + \beta_4 OWN_{it} + \epsilon_{it}$$

Estimation Technique

The study employs:

- Panel Ordinary Least Squares (OLS)
- Fixed Effects Model
- Random Effects Model

The Hausman specification test determines the appropriate estimator.

Reliability and Validity Measures

To ensure empirical robustness:

- Multicollinearity tested using Variance Inflation Factor (VIF)
- Heteroskedasticity checked via Breusch–Pagan test
- Autocorrelation corrected using robust standard errors
- Endogeneity concerns addressed through lagged variables

5. Empirical Results

5.1 Descriptive Statistics

Trends in Governance Compliance Post-2013. The descriptive analysis provides a first glimpse into how Indian listed companies adapted to the changes that have been made in company governance since the Companies Act 2013. The study analyzes governance metrics after the reforms and the type of governance management, board composition, audit management and disclosure practices to examine the extent to which companies are still in compliance. Compliance on the NSE-listed companies is high after the reforms. Companies with independent directors rose very high in the first two years after the regulations were enforced. Moreover, the fact that companies were forced to appoint women directors means that the board of large firms has as well.

5.2 Key descriptive trends are:

- The percentage of independent directors rose steadily with compliance with the laws.
- The group is more independent: As a result, companies are now more likely to have an audit committee that is completely independent if they are a big company or a local affiliate.
- The risk reporting, CSR disclosure, and related party transaction explanations are more transparent in the annual report.
- Businesses and multinational affiliates are more likely to adopt governance systems than mid-sized and promoter companies.

Despite an increase in compliance metrics, there are still variations in industry sectors. Family-owned firms often failed to meet minimum legal standards, but also did not voluntarily comply with governance standards, meaning there is a chance for compliance-driven rather than culture-based reform of companies.

Correlation matrix and multicollinearity diagnosis. The correlation matrix was developed to identify correlations between the governance variables and financial performance parameters before regression was performed. This work was conducted in twofold manner:

- To identify strong associations between governance qualities and the firm's performance.
- To avoid the presence of unhealthy multicollinearity among the variables.

The correlation results indicate that:

- Positive correlation between board diversity, audit committee independence and ROA.
- Negative correlation between leverage and profitability.
- There is moderate correlation between firm size and governance quality, meaning that larger firms have more resources to comply.

Variance Inflation Factor (VIF) statistics were below the traditional threshold, indicating that multicollinearity is not a factor in the estimation of coefficients. Governance variables thus capture more than one dimension of the institutional environment. Regression analysis: Governance and Financial performance. The regression results for the panel show that governance compliance is measurable in terms of financial results.

Model 1: Governance and ROA.

We found that board gender diversity is positively correlated with ROA and statistically significant when compared to the control group. Firms with diverse boards show better operational efficiency, possibly due to better monitoring, more strategic thinking and stronger stakeholder ownership. The board size has mixed effects in the model and too large boards may not help in decision-making efficiency. Firm size is positively related to performance as economies of scale and institutional maturity are strong. In conclusion, the findings indicate that governance reforms under the Companies Act 2013 are more than mere symbolic but are beneficial for the company business.

Model 2: Audit committee independence and earnings management.

The second model looks at whether audit committee independence limits opportunistic financial reporting behaviour. The results show that:

- Audit committee independence is highly negative for earnings management proxy.
- A lower discretionary accrual with independent audit committee.
- Strong monitoring mechanisms reduce managerial discretion over accounting choices. These findings therefore reinforce the monitoring hypothesis of corporate governance and show that audit oversight mechanisms are effective in reducing information asymmetry. Endogeneity Testing: Addressing Reverse Causality

A central concern in governance-performance research is **endogeneity**—whether better-performing firms simply adopt stronger governance structures rather than governance causing improved performance.

To address this difficulty, our econometric methods were developed:

Two-Stage Least Squares (2SLS): In the first stage we used the lagged governance scores and industry governance averages to predict governance quality. In the second stage we used the predicted governance

values to estimate the effect of governance on performance. The results are still statistically significant, and governance improvements are independent of one another and do not correspond to the reverse causality.

Generalized Method of Moments (GMM): The dynamic panel estimation method using GMM further controlled for:

- Unobserved firm heterogeneity.
- Persistence of firm performance.
- Simultaneity bias.

Diagnostic tests confirm instrument validity and no over-identification problems. The consistency of the results of OLS, Fixed Effects, 2SLS, and GMM models strengthens the evidence for the empirical findings.

6. Discussion of findings

The “Independent Director” Paradox. While regulatory reforms promote board independence, the Indian corporate environment is a paradox. Many listed companies are still promoter-driven, and controlling shareholders are still in control of the selection of directors. Independent directors are required to take on legal and ethical duties and are required to comply with the law, but the degree of independence they achieve may be limited by:

- Social and professional connections with promoters.
- Limited access to firm-specific information.
- Cultural reluctance to challenge dominant shareholders may make up the difference between legal independence and behavioural independence.

We have shown that independent directors can improve reporting quality but they are not always effective and their effectiveness varies across ownership structures. As such, a true governance reform is about institutional autonomy and not about increasing the number of independent directors. Investor perception and market reaction. Investors are more likely to reward a particular kind of governance characteristic more strongly than others in market valuation. Investors are most inclined to:

- Transparent disclosure practices
- Independent audit committees.
- Board diversity signals.

Capital markets view these qualities as credible signatures of reduced governance risk. Better governance reduces perceived agency costs, boosts earnings credibility, and minimizes information asymmetry. Interestingly, gender diversity requirements attracted positive responses from markets even when operational performance improvement was slow. This suggests that governance reforms are reputational signals of investor sentiment.

7. Conclusion & Policy Implications

The findings from the empirical analysis show that the reforms in the framework of the **Companies Act, 2013** have led to measurable improvements in financial performance, transparency, and quality of reporting of Indian listed companies. Board diversity and independence of the audit committee is an important determinant of what makes governance effective. Policy implications for regulators.

Regulatory bodies such as the Securities and Exchange Board of India and the Ministry of Corporate Affairs may consider the following interventions: 590

- Enhancing the monitoring mechanism to identify “shadow directors” who influence the process without any formal responsibility for the directors.
- Increasing disclosure requirements for director independence evaluation.
- Introducing governance performance audits rather than compliance-based reporting alone.

Improvement in the training and certification process for independent directors for operational effectiveness.

Implications for Investors. For investors with an investment horizon in emerging markets, governance indicators must be viewed in conjunction with other indicators beyond just financial ratios:

- Excessive promoter control or related-party transactions.
- Interlocks of directors in various groups of companies.
- Nominally independent directors lacking professional diversity.

Weak audit committee participation or financial expertise gaps. A better understanding of these governance “red flags” can assist investors to better assess the sustainability of the firm long term. While the study has some merits, it has some drawbacks: We only look at listed companies and not companies with unlisted subsidiaries, for which there might be more governance issues in place. We measure governance quality through an observable disclosure process that could not be used to fully appreciate informal power relationships. Data availability limitations restrict the study of behavioural interactions in boardrooms.

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