**Corporate Governance Practices in Banking Sector: A Comparative study of selected banks**

**Rohit Kumar & Zeeshan \*, Prof. Miss Vaishali Joshi**

SCHOOL OF FINANCE & COMMERCE GALGOTIAS UNIVERSITY

**ABSTRACT**

The abstract highlights the significance of corporate governance (CG) in ensuring corporate excellence and integrity, especially in the wake of past corporate crises and scandals. In India, the importance of CG was underscored by events such as the Harshad Mehta stock scam in 1992 and the Satyam Software Services Ltd. fraud in 2009. Legislative initiatives such as the Companies Act of 2013 aimed to strengthen CG mechanisms to prevent corporate mismanagement and scandals. The study focuses on analyzing and comparing the CG frameworks of eight major Indian banks, categorized into Public Sector Banks (PuSB) and Private Sector Banks (PvSB). Data was collected from the banks' latest annual reports, focusing on parameters like board composition, mandate, and committee activities. Results indicate that ICICI Bank Ltd. demonstrates higher levels of independence and transparency among PvSBs, while State Bank of India (SBI) exhibits proactive CG practices among PuSBs, particularly through the active involvement of non-executive independent directors across various board committees.

# ACKNOWLEDGEMENT

We are thrilled to present the report of our MBA extension project completed during the last year of our MBA program. Our heartfelt gratitude goes to Ms. Vaishali for her consistent guidance and motivation.

We also want to acknowledge the support and assistance of the office staff members during the development of our project. Lastly, we appreciate the contribution of our friends towards the successful completion of the extension.

**Introduction**

The introduction discusses the evolution and significance of corporate governance (CG), particularly in the context of the banking sector. CG is crucial for achieving organizational goals and protecting against failures and fraud. It encompasses both internal (board structure, governance) and external (shareholders, stakeholders) aspects of a company, ensuring effective controls, governance structures, performance measurement, and succession planning. Global experiences, including corporate scandals like Enron and Satyam, underscore the importance of stringent CG regulations to prevent future failures and frauds. The introduction also highlights the historical development of CG globally and its increasing importance in India, especially after incidents like the Harshad Mehta scam and the Satyam fraud. Legislative initiatives such as the Companies Act of 2013 in India aim to strengthen CG mechanisms in response to corporate mismanagement and scandals.

**Need for research**

The need for research on bank corporate governance is crucial due to several reasons:

1. Importance of Banking: Banks are pivotal to all economies, serving as the backbone of financial systems by facilitating financial transactions and resource allocation.
2. Transparency and Public Trust: Banks hold public deposits and have social responsibilities. Good governance practices enhance transparency and public confidence in the banking system.
3. Risk Reduction and Efficiency: Effective governance structures mitigate risks such as fraud and mismanagement, safeguarding depositors' funds and promoting efficient resource allocation.
4. Comparative Analysis: Comparing governance practices among public and private banks or across different countries reveals strengths and weaknesses, informing future strategies.
5. Research Contribution: Research in this area provides valuable insights into how banks can adopt best practices, benchmarking them to identify areas for improvement and highlight successful approaches. Overall, such research strengthens and enhances the stability of the banking sector.

**Scope of your research**

1. **Board Composition and Operations:**
	* Examine diversity, expertise, independence, roles, and meeting effectiveness of boards.
2. **Risk Management Practices:**
	* Compare methods for identifying and mitigating risks, and evaluate internal controls and compliance.
3. **Transparency and Disclosure:**
	* Assess financial reporting transparency, clarity of stakeholder information, and communication channels.
4. **Compensation Practices:**
	* Compare executive pay structures, risk-linked allowances, and the role of compensation committees.

**Comparative Analysis:**

* **Bank Selection:** Include public vs. private banks, banks from different regulatory environments, and various sizes and business models.
* **Metrics and Methodology:** Use industry standards, quantitative data, and optional qualitative interviews to analyse governance strengths and weaknesses.

**Additional Considerations:**

* **Regulatory Landscape:** Overview of governance regulations in selected regions.
* **Impact Analysis:** Investigate the impact of governance practices on performance and risk profile.

**Deliverables:**

* Provide a detailed comparative study with evidence-based arguments.
* Offer recommendations for improvements and highlight best practices.

**Top of Form**

**Literature Review**

Numerous studies on corporate governance (CG) in India highlight various factors influencing firm performance:

1. **Board Size and Composition:**
	* Kathuria and Sprint (1999) found that increasing board size improves financial performance but has diminishing returns with company size.
	* Chugh, Meador, and Kumar (2011) concluded larger boards improve financial performance, but too much independence can reduce it.
	* Thomas and Thakur (2014) and Hussein and Venkatram (2013) found smaller boards and more independent directors enhance performance.
2. **Ownership Structure:**
	* Kumar (2004) showed ownership by institutional investors and directors impacts performance non-linearly.
	* Dwivedi and Jain (2005) found external ownership positively affects shareholder value, while managerial ownership has a negative impact.
	* Emmanuel and Hodo (2012) and Mohammed (2012) found board size and shareholder number positively impact performance in Nigerian banks.
3. **Executive Compensation:**
	* Abdullah (2006) found no link between executive pay and profitability in Malaysian firms.
	* Narwal and Jindal (2015) found a strong positive relationship between executive compensation and profitability in the Indian textile industry.
4. **Transparency and Disclosure:**
	* Mohd. and Fatima (2009) linked better disclosure and transparency scores with higher market value and performance.
	* Gowd, Kiran, and Rao (2013) found positive relationships between sales, market capitalization, profit, and CG score in SBI.
5. **Sector-Specific Studies:**
	* Adnan et al. (2011) found smaller boards and higher ownership rates improve efficiency in Malaysian banks.
	* Pandya (2011) found significant links between CG structures, board independence, CEO duality, and performance in Indian banks.
	* Stefano and Olatunji (2011) found more external directors negatively impact financial performance.
6. **Other Findings:**
	* Al-Musalli and Ismail (2012) explored factors influencing intellectual capital in GCC banks.
	* Vishwakarma and Alok (2015) found board size, independence, and committees significantly impact IT companies' financial performance in India.

**Research Gaps**

* Insufficient benchmarking between public sector (PuSB) and private sector banks (PvSB) in India.
* Limited studies focusing comprehensively on the Indian banking sector.
1. Risk Reduction and Efficiency: Effective governance structures mitigate risks such as fraud and mismanagement, safeguarding depositors' funds and promoting efficient resource allocation.
2. Comparative Analysis: Comparing governance practices among public and private banks or across different countries reveals strengths and weaknesses, informing future strategies.
3. Research Contribution: Research in this area provides valuable insights into how banks can adopt best practices, benchmarking them to identify areas for improvement and highlight successful approaches. Overall, such research strengthens and enhances the stability of the banking sector.

**Objectives**

This study has established the following main objectives to achieve the results through this study.

1. Compare selected key CG practices mentioned in PvSB and PuSB.

2. Investigating the salient features of CG in the Indian banking sector.

3. A critical study on the evolution of CG practices in the Indian banking sector.

4. Evaluate the key steps taken by the banking sector towards effective CG.

**Research Methodology Summary**

This study analyzed eight major Indian banks: four public sector banks (SBI, Bank of Baroda, Punjab National Bank, and United Bank of India) and four private sector banks (Dhan Laxmi Bank, DCB Bank, ICICI Bank, and Lakshmi Vilas Bank). The sample was chosen based on market value and founding year. The study period is 2015-16, using data from the financial year 2015-16 annual reports and bank websites. The focus was on the "governance" section of the annual reports, examining key parameters such as the composition, mandate, and meeting frequency of the Board, Risk Management Committee, Control Committee, Shareholders' Committee, Remuneration Committee, and CSR Committee.

 **Table-1: Brief Description of Sample Selected under the Study**

|  |  |  |
| --- | --- | --- |
| **Name of Bank** | **Year of establishment** | **Market Capitalisation** (INR) |
| **Private sector Bank** |  |  |
| Dhan Laxmi Bank ltd. | **August 1994** | 11.77 Lakhs Crore |
| Laxmi Vilas Bank Ltd. | **1994** | 7.70 Lakhs Crore |
| DCB Bank Ltd. | **November 1985** | 3.56 Lakhs Crore |
| ICICI Bank Ltd. | **1993** | 3.24 Lakhs Crore |
| IndusInd Bank | **April, 1994** | 1.20 Lakhs Crore |
| **Public Sector Bank** |  |  |
| State bank of India | **July 1995** | 6.75 Lakhs Crore |
| Bank of Baroda | **July 1908** | 1.37 Lakhs Crore |
| Punjab National Bank | **May 1894** | 1.38 Lakhs Crore |
|  Indian Overseas | **Feb 1937** | 1.13 Lakhs Crore |
| United Bank of India | **Nov 1950** | 1.0 Lakhs Crore |

 **Source:** From the official site of Bank and research firm like Money control

**Data Analysis and Results**

In order to understand the discharge practices and status of the selected banks, important parameters such as board structure, composition of key committees and frequency of meetings including audit committee, risk management committee, stakeholder committee, remuneration committee and board committee are analysed. The data analysis and results are explained below:

**Case Structure Summary**

The study focuses on the role and composition of boards in corporate governance across eight major Indian banks, split between public sector banks (PuSB) and private sector banks (PvSB). Key points include:

1. **Board Composition:**
	* **CEO:** Primary role is directing and managing the business.
	* **Non-Executive Director (NED):** External, not involved in daily management, acts as an overseer and whistle-blower.
	* **Independent Director (ID):** A type of NED with no ties to the company, ensuring good governance.
2. **Regulatory Requirements:**
	* Clause 49 mandates that at least 50% of board members must be non-executives if the chairman is a NED; if the chairman is an ED, at least 50% must be independent directors.
3. **Board Composition in Selected Banks:**
	* **Private Banks (PvSB):** Lakshmi Vilas Bank (LVB) has the highest board independence with 92% NEDs.
	* **Public Banks (PuSB):** United Bank of India leads with 67% NEDs; UBI has 44% IDs, while DCB has 77%.
	* **Highest Executive Directors (EDs):** ICICI (PvSB) at 38%, and Bank of Baroda (PuSB) at 30%.
4. **Board Meetings:**
	* **Frequency:** DCB Bank held the fewest meetings (7 per year).
	* PvSB typically have NEDs as chairmen, while PuSB often have EDs.
5. **Women Directors:**
	* All banks meet the statutory requirement for women directors.

This analysis highlights the varied board structures and governance practices between public and private sector banks, reflecting their approaches to regulatory compliance and governance efficacy.

 **Table-II: Analysis of Board Composition**

|  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **Name of Bank** | **Total Directors** | **Non-executive directors****Excluding Chairman**  | **Independent Non-Executive Director** | **Woman Non-Executive Directors** | **Executive Director****Excluding Chairman** | **Woman Executive Director** | **Number of Board Meeting** | **Is Chairman Executive** |
| **Private Sector Bank** |  |  |  |  |  |  |  |  |
| Dhan Laxmi Bank Ltd | **11** | **10** | **6** | **1** | **1** | **0** | **12** | **No** |
| DCB Bank Ltd. | **13** | **11** | **10** | **1** | **1** | **0** | **7** | **No** |
| ICICI Bank Bank | **13** | **7** | **7** | **0** | **5** | **2** | **10** | **No** |
| Axis Bank Ltd. | **13** | **0** | **8** | **2** | **0** | **0** | **13** | **Yes** |
| Laxmi Vilas Bank Ltd. | **12** | **11** | **6** | **1** | **0** | **0** | **12** | **No** |
| **Public Sector Bank** |  |  |  |  |  |  |  |  |
| State bank of India | **14** | **5** | **4** | **1** | **4** | **1** | **12** | **Yes** |
| Bank of Baroda | **10** | **2** | **4** | **1** | **3** | **0** | **13** | **No** |
| Punjab National Bank | **11** | **7** | **4** | **1** | **3** | **1** | **13** | **Yes** |
|  Indian Overseas | **10** | **1** | **0** | **1** | **2** | **1** | **10** | **Yes** |
| Union Bank of India | **9** | **6** | **4** | **1** | **2** | **0** | **10** | **Yes** |

 **Source:** Compiled by author from Annual Report 2015-16 of respective Banks (2016)

**Audit Committee Analysis (2015-16)**

* Role: Ensures the accuracy, adequacy, and reliability of financial accounts.
* Meeting Requirement: At least four times a year.

**Key Findings:**

* Highest Independence: ICICI (100% independent directors), SBI (50%).
* Lowest Independence: LVB (50%), PNB (20%).
* Most Meetings: Bank of Baroda with 12 meetings per year.

**Risk Management Committee Analysis (2015-16)**

Role: Assists the board in identifying, assessing, and mitigating key, operational, and external risks.

Key Findings:

• Highest Independence in PvSB: DCBL with 80% independent directors.

• Highest Independence in PuSB: SBI with 50% independent directors.

• Lowest Independence: LVB (33%), PNB (17%).

• Most Meetings: ICICI held the highest number of meetings during the year.

**Table-III: Analysis of Audit Committee and Risk Management Committee**

|  |  |  |
| --- | --- | --- |
| **Name of Bank** | **Audit Committee** | **Risk Management Committee** |
|  |  |
| **Total Directors** | **No. of ID** | **No. of ED** | **No. of Meeting** | **No of meeting**  | **No of meeting** | **No of meeting** | **No of meeting** |
| **Private Sector Bank** |  |  |  |  |  |  |  |  |
| Dhan Laxmi Bank Ltd | **5** | **4** | **1** | **8** | **3** | **2** | **1** | **4** |
| DCB Bank Ltd. | **5** | **3** | **0** | **5** | **5** | **4** | **1** | **4** |
| ICICI Bank Bank | **4** | **4** | **0** | **8** | **7** | **5** | **1** | **7** |
| Axis Bank Ltd. | **5** | **5** | **0** | **8** | **6** | **5** | **1** | **7** |
| Laxmi Vilas Bank Ltd. | **6** | **3** | **0** | **8** | **6** | **2** | **2** | **4** |
| **Public Sector Bank** |  |  |  |  |  |  |  |  |
| State bank of India | **8** | **4** | **2** | **11** | **8** | **4** | **2** | **4** |
| Bank of Baroda | **5** | **2** | **1** | **12** | **5** | **1** | **3** | **5** |
| Punjab National Bank | **5** | **1** | **1** | **5** | **6** | **1** | **4** | **4** |
|  Indian Overseas | **4** | **1** | **1** | **1** | **5** | **1** | **3** | **3** |
| United Bank of India | **7** | **3** | **1** | **9** | **NA** | **NA** | **NA** | **NA** |

**Stakeholder Relations Committee Analysis**

* **Role:** Manages shareholder relations, including share recognition, transfer, and handling shareholder queries/complaints.

**Key Findings:**

* **Highest Independence in PvSB:** DCBL with 100% independent directors.
* **Highest Independence in PuSB:** SBI and UBI, both with 60% independent directors.
* **Lowest Independence:** DBL (33%), PNB (25%).
* **Most Meetings:** PNB held the highest number of committee meetings among all the banks studied.

**Corporate Social Responsibility (CSR) Committee Analysis**

* Role: Oversees social sector development activities, ensuring compliance with the CSR policy under the Companies Act, 2013. Tasks include reviewing social activities, formulating policies, and monitoring implementation and compliance.
* Key Findings:
* Highest Independence in PvSB: DCBL with 60% independent directors.
* Highest Independence in PuSB: Only SBI has a CSR committee with 67% independent directors.
* Most Meetings: SBI and LVB held the highest number of CSR committee meetings among the selected banks.

**Table-IV: Analysis of the Stakeholder Relationship Committee and CSR Committee**

|  |  |  |
| --- | --- | --- |
| **Name of Bank** | **Stakeholder Relationship Committee** | **CSR Committee** |
| **Numbers of Members** | **No. of ID** | **No. of ED** | **No. of Meeting** | **No of meeting**  | **No of meeting** | **No of meeting** | **No of meeting** |
| **Private Sector Bank** |  |  |  |  |  |  |  |  |
| Dhan Laxmi Bank Ltd | **3** | **1** | **1** | **4** | **3** | **1** | **1** | **1** |
| DCB Bank Ltd. | **3** | **3** | **0** | **4** | **5** | **3** | **1** | **2** |
| ICICI Bank Bank | **3** | **2** | **1** | **4** | **4** | **2** | **1** | **3** |
| Axis Bank Ltd. | **5** | **5** | **0** | **4** | **4** | **3** | **1** | **2** |
| Laxmi Vilas Bank Ltd. | **5** | **2** | **0** | **3** | **5** | **1** | **2** | **4** |
| **Public Sector Bank** |  |  |  |  |  |  |  |  |
| State bank of India | **5** | **3** | **2** | **4** | **6** | **4** | **2** | **4** |
| Bank of Baroda | **4** | **2** | **2** | **4** | **No** |  |  |  |
| Punjab National Bank | **4** | **1** | **3** | **6** | **No** |  |  |  |
|  Indian Overseas | **4** | **1** | **1** | **1** | **No** |  |  |  |
| United Bank of India | **5** | **3** | **2** | **4** | **No** | **NA** | **NA** | **NA** |

**Source:** Compiled by author from Annual Report 2015-16 of respective Banks (2016)

**Compensation Committee**

The foremost imperative work of the Recompense Committee is to authorize official stipend, trade and other benefits. Examination of information from the chosen banks appears that ICICI and SBI are the foremost free, naming an autonomous chief for 100% and 50% of the committee composition. On the other hand, PNB's recompense committee has as it were 25% free executives, taking off small freedom (see Table 5).

**Table V: Remuneration Committee Analysis.**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Name of Bank** | **Numbers of Member** | **No. of ID** | **No. of ED** | **No. of ED** |
| **Private sector Bank** |  |  |  |  |
| Dhan Laxmi Bank ltd. | **3** | **2** | 0 | 4 |
| Laxmi Vilas Bank Ltd. | **4** | **3** | 0 | 5 |
| DCB Bank Ltd. | **4** | **3** | 1 | 3 |
| ICICI Bank Ltd. | **3** | **3** | 0 | 8 |
| IndusInd Bank | **3** | **3** | 0 | 4 |
| **Public Sector Bank** |  |  |  |  |
| State bank of India | **4** | **2** | 0 | 1 |
| Bank of Baroda | **5** | **2** | 0 | 2 |
| Punjab National Bank | **4** | **1** | 0 | 1 |
|  Indian Overseas | **4** | **1** | 0 | 1 |
| United Bank of India | **5** | **2** | 0 | 1 |

 **Source:** Compiled by author from Annual Report 2015-16 of respective Banks (2016)

**Board**

The board usually deals with all matters within the competence of the central board. This may include real estate, insurance, commercial and PandL topics etc. Based on the available data of the selected banks, it is observed that SBI and LVB held the highest number of committee meetings in the respective group of banks during the year. banks (see Table 6).

**Table VI: Board Committee Analysis: Board Management.**

|  |  |  |
| --- | --- | --- |
| **Name of Bank** | **Numbers of Members** | **No. of Meetings** |
| **Private sector Bank** |  |  |
| Dhan Laxmi Bank ltd. |  **4** | 11 |
| Laxmi Vilas Bank Ltd. | **10** | 19 |
| DCB Bank Ltd. | **4** | 1 |
| ICICI Bank Ltd. | **NA** | NA |
| IndusInd Bank | **4** | 1 |
| **Public Sector Bank** |  |  |
| State bank of India | **4+** | 52 |
| Bank of Baroda | **6** | 21 |
| Punjab National Bank | **7** | 18 |
|  Indian Overseas | **6** | 20 |
| United Bank of India | **NA** | NA |

 **Source:** Compiled by author from Annual Report 2015-16 of respective Banks (2016)

Top of Form **Limitations**

1. **Sample Size Constraints and Generalizability:**
* **Limited Sample Size:** A smaller sample of banks might limit the generalizability of findings to the entire population, especially if not diverse enough.
* **Mitigation Strategies:** Efforts made to select a diverse sample, capturing variations in bank size, type, location, and regulatory environments.Top of Form

**2. Data Availability, Accuracy, and Potential Biases:**

* **Data Availability and Completeness:** Annual reports and regulatory filings may not offer a complete view of governance practices, potentially masking weaknesses.
* **Interview Limitations:** Interviews with bank personnel may be constrained by their willingness to share sensitive information or biases, possibly understating governance issues.
* **Mitigation Strategies:** Efforts to triangulate data using multiple sources (interviews, documents, industry reports) to ensure a comprehensive understanding of governance. Acknowledgment of potential biases in interviews and measures like anonymity to encourage candid responses. Validation of interview data with corroborating evidence from other sources.

**3. Time Constraints and Research Scope:**

* **Time Constraints:** Limited time may restrict the depth of analysis.
* **Mitigation Strategies:** Focus on specific areas of corporate governance and acknowledge the need for future research to explore other aspects.

**4. Selection Bias and Representativeness:**

* **Selection Criteria Bias:** Criteria used to select banks may introduce bias.
* **Mitigation Strategies:** Justify selection criteria and emphasize the value of the chosen sample while acknowledging potential limitations.

**5. External Factors and Challenges in Establishing Causality:**

* **External Factors:** Difficulty in establishing a direct causal relationship between governance practices and bank performance.
* **Mitigation Strategies:** Focus on identifying correlations and employ statistical analysis while acknowledging the influence of external factors.

**6. Methodological Limitations:**

* **Chosen Methodology Limitations:** Interviews and document analysis have inherent limitations.
* **Mitigation Strategies:** Discuss strengths and weaknesses of methodologies, ensure objectivity, and triangulate data from various sources.Top of Form

**Corporate Governance Practices in the Indian Banking Sector:**

1. **Composition and Structure of the Board:**
	* Boards comprise senior executives and external directors.
	* Responsible for strategic direction, oversight, and compliance with laws and regulations.
	* Appoints key personnel and evaluates their performance.
2. **Independent Directors:**
	* Play a crucial role in ensuring transparency, accountability, and objectivity.
	* Regulated by the Companies Act, 2013, and SEBI regulations.
	* Expected to bring diverse expertise and impartial monitoring, especially in risk management and compliance.
3. **Risk Management:**
	* Essential for the stability and sustainability of banks.
	* Governed by comprehensive guidelines issued by the RBI.
	* Banks must have robust risk management systems covering various risks such as credit, market, liquidity, and operational.
	* Risk management committees oversee risk management practices and ensure compliance with regulatory requirements.

**Disclosure, Transparency, Internal Controls, and Audit:**

**Disclosure and Transparency:**

* Essential for maintaining trust and confidence in the banking sector.
* Banks must disclose important information to shareholders, regulators, and stakeholders in a timely and transparent manner.
* Disclosure requirements include financial statements, annual reports, and other material information affecting stakeholders.
* SEBI's disclosure standards mandate transparency in corporate governance practices and related-party transactions.

**Internal Controls and Audit:**

* Crucial for ensuring compliance, safeguarding assets, and preventing fraud.
* Banks must establish effective internal control mechanisms, including policies, procedures, and systems for financial reporting, risk management, and compliance.
* Internal audit functions independently evaluate the effectiveness of internal controls and provide assurance to the board and senior management.

**Conclusion Summary:**

The study focused on the composition and autonomy of key board committees (risk management, corporate responsibility, audit, compensation, and stakeholder grievance) in selected public (PuSB) and private sector banks (PvSB) in India.

**PvSB Findings:**

**ICICI Bank:** Maintains a high level of autonomy in board committees, standing out among private sector banks.

**DBL:** Lacks significant autonomy in its board committees.

**PuSB Findings:**

**SBI:** Proactive with substantial involvement of non-executive independent directors in board committees.

**PNB:** Has less autonomy, with a high percentage of CEOs in board committees.

**General Observations:**

**Frequency of Meetings:** ICICI and SBI held the most frequent board committee meetings, reflecting proactive governance.

The study suggests other banks should reconsider their board structures to align with the 2013 Companies Act, enhancing the inclusion of independent directors for better governance.