INVESTOR'S PERCEPTION ABOUT NON-FINANCIAL INFORMATION

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Introduction

With the internationalization of cross-border portfolios, and the financial crisis that have occurred in many parts of the world, investors and institutional investors in particular, increasingly look more carefully at the non financial information of the company particularly the corporate governance practices of companies and its corporate social responsibility information.

Investor

- Investor is one who commits money to investment products with the expectation of financial return.
- The products an investor may buy range widely, but include stocks, bonds, real estate, commodities, and collectibles (e.g. art). The portfolio of an investor commonly includes a variety of assets that balance the rewards and risks of each investment. An investor is distinguished from a speculator, who seeks to make quick, large gains from price increases on risky assets.
- Investor is of two types

1. Natural Person
2. Legal Person

Perception

- Perception is the process of attaining awareness or understanding of the environment by organizing and interpreting sensory information. All perception involves signals in the nervous system, which in turn result from physical stimulation of the sense organs.

Investor Perception

- Investor perception about a company would mean how the investor envisions or sees the company.
- Knowledge of Investor Perception is important for a company because:
  - The perceptions of investors can influence the company's corporate strategy and the investment proposition
  - The insights measure the level of understanding of the company, gauge sentiment and highlight the degree of support
  - The feedback shapes, amends and reinforces the company's message to the market
  - The strategic findings of an annual investor perception study complement the tactical day-to-day feedback provided by corporate brokers
  - Listening and responding demonstrates awareness, responsibility and good corporate governance

Investor Protection

- Is the combination of efforts and activities to observe safeguard and enforce the rights and claims of a person in his role as an investor. This includes advice and legal action.
- The assumption of a need of protection is based on the experience that financial investors are usually structurally inferior to providers of financial services and products due to lack of professional knowledge, information and/or experience.
- All outside investors, whether large or small, shareholders or creditors need to have their rights protected.

SEBI and Investor Protection

- Securities Exchange Board of India (SEBI) was established with the primary objective of protecting the interest of the investors in the securities market
- With this objective, SEBI issued the SEBI (Disclosure and Investor Protection) Guidelines, 2000.
- SEBI can issue directions to all intermediaries and other persons associated with the securities market in the interest of the investors or for orderly development of the securities market
- SEBI has notified the SEBI (Investor Protection and Education Fund) Regulations, 2009

SEBI Investor Protection and Education Fund

The fund shall be used for the following purposes:-

- Educational activities including seminars, training, research and publications, aimed at investors
- Awareness programmes through media - print, electronic, aimed at investors
- Funding investor education and awareness activities of investor associations recognized by the Board
- Aiding investor associations recognized by the Board to undertake legal proceedings in the interest of investors in securities that are listed or proposed to be listed

Investor Grievance Redressal Mechanism

- SEBI and Stock Exchanges have set up investor grievance redressal cells for fast Redressal of investor complaints relating to securities markets
- SEBI has set up a mechanism for redressal of investor grievances arising from the securities market
- SEBI provides "walk-in" service at its head office at Mumbai and its regional offices at New Delhi, Chennai, Kolkatta and Ahmedabad on all working days. Investors can meet the officials and get guidance relating to the grievances that they may have against issuers. Investors can also meet the higher officials of SEBI on specified working days.

Investor Protection and Enhanced Corporate Governance u/Companies Bill 2011

- Protection for Minority Shareholders:

(a) Exit option to shareholders in case of dissent to change in object for which public issue was made.

(b) Specific disclosure regarding effect of merger on creditors, key managerial personnel, promoters and non-promoter shareholders is being provided. The Tribunal is being empowered to provide for exit offer to dissenting shareholders in case of compromise or arrangement.

(c) The Board may have a director representing small shareholders who may be elected in such manner as may be prescribed by rules.

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- Investor Protection:

(a) Acceptance of deposits from public subject to a more stringent regime.

(b) Central Government to have power to prescribe class or classes of companies which shall not be permitted to allow use of proxies. The Bill also to have provisions to provide that a person shall have proxies for such number of members /such shares as may be prescribed.

(c) Issue and transfer of securities and non-payment of dividend by listed companies, has to be administered by SEBI by making regulations.(Clause 24)

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(d) An act of fraudulent inducement of persons to invest money is punishable with imprisonment for a term which may extend to ten years and with fine which shall not be less than the amount involved in fraud, but which may extend to three times the amount involved (Clause 36 & 447).

(e) Provisions for Class Action Suits revised to provide minimum number of persons who may apply for such suits. Safeguards against misuse of these provisions also being included.
A suit may be filed by a person who is affected by any misleading statement or the inclusion or omission of any matter in the Prospectus or who has invested money by fraudulent inducement (Clause 37).

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- Enhanced Corporate Governance
- Powers have been given to Courts and Tribunals to re-open accounts
- Serious Fraud Investigation Office has been designated as the main investigating agency for frauds relating to companies.
- Mandatory Internal audit for specific companies
- Provides for provisions for better disclosure like statement of compliances of all laws in board reports, more disclosures in financial statements and includes associated companies and joint ventures in the ambit of consolidated accounts.

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- Mandates applicability of postal ballot for private companies, introduces auditing and secretarial standards, envisages mandatory appointment of independent directors and further mandates the requirement of quorum of a general meeting based on number of members in the company.
- Has introduced the concept of Class Action Suits with an aim to strengthen the rights of minority stakeholders, , which are already well established in countries like the UK and the US.

Non financial Information

- Industry cohort measurements of performance linked to non-financial value indicators
- Industry cohort measurements is information that contextualizes performance against peers e.g market share, quality rankings, customer satisfaction survey data etc
- Corporate Governance Information
- Corporate Social Responsibility Information

Non Financial Disclosure

- CARO Report
- Research & Development
- Fraud & Corruption
- Strategic Plan
- Indicators of economic performance
- Key relationship with employees, suppliers
- Board of Directors Report
- Product Innovation
- Corporate Governance Report
- Risk Management Framework
- Environment Policy

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- Compliance with Laws
- CSR (Corporate Social Responsibility) Report
- Strategic Decisions
- Industry Perspective (National & Global)
- Customer Information
- Key Management Personnel
- Human Resource

Core Non financial Drivers

- Human Capital – Employees engagement
- Customer Relation- customer satisfaction
- Partnerships- Public perception, supply chain management
- Environment- Carbon emissions, waste management, life cycle assessment
- Innovation- Product/service development
- Corporate Governance- Ethical integrity , board composition

Financial Information

- Record of the financial activities of a business, person, or other entity.
- **Statement of Financial Position**: also referred to as a balance sheet, reports on a company's assets, liabilities, and ownership equity at a given point in time.
- **Statement of Comprehensive Income**: also referred to as Profit and Loss statement (or a "P&L"), reports on a company's income, expenses, and profits over a period of time. A Profit & Loss statement provides information on the operation of the enterprise. These include sale and the various expenses incurred during the processing state.

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- **Statement of Changes in Equity**: explains the changes of the company's equity throughout the reporting period
- **Statement of cash flows**: reports on a company's cash flow activities, particularly its operating, investing and financing activities.

Financial Drivers

- Reduced costs
- Increased sales
- Increased cash flow
- Brand value
- Risk Management

Other Information

- This information is part of financial statements. It provides detail information on its nature, relation and type of activity.
- **Examples**

1. Management Remuneration
2. Analytical Ratios
3. Research Expenses
4. Certain other expenses
5. Notes to Accounts

GAAP (Generally Accepted Accounting Principles)

- Collection of rules and procedures and conventions that define accepted accounting practice; includes broad guidelines as well as detailed procedures
- Common set of accounting principles, standards and procedures that companies use to compile their financial statements. GAAP are a combination of authoritative standards (set by policy boards) and simply the commonly accepted ways of recording and reporting accounting information.
- GAAP cover things such as revenue recognition, balance sheet item classification and outstanding share measurements.

Corporate Governance

- The principles of Governance have been in existence for centuries.
- History reveals that Kautilya also called Chanakya in 300 BC propounded principles of good governance. In his celebrated treatise on statecraft “Arthashastra”, he provided principles of governance. He states the fourfold duty of a King as: Raksha (Protection), Vriddhi (Enhancement), Palana (Maintenance). Yogakshema – (Safeguard)

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- These four principles can be elaborated in the modern context as:

1. Protecting shareholders wealth;
2. Enhancing the wealth through proper utilization of assets;
3. Maintenance of that wealth and not frittering away in unconnected and non profitable ventures or through appropriation; and
4. Safeguarding the interests of the shareholders

Meaning of Corporate Governance

- Corporate Governance is a broad concept and has been defined and understood differently by different groups and at different points of time.
- The Cadbury Committee - "the system by which companies are directed and controlled". It is generally understood as the framework of rules, relationships, systems and processes within and by which authority is exercised and controlled in corporations."
- The Kumar Mangalam Birla Committee report - "…fundamental objective of corporate governance is the 'enhancement of the long-term shareholder value while at the same time protecting the interests of other stakeholders."

Need for good Corporate Governance

- It lays down the framework for creating long-term trust between companies and the external providers of capital
- It improves strategic thinking at the top by inducting independent directors who bring a wealth of experience, and a host of new ideas
- It rationalizes the management and monitoring of risk that a firm faces globally
- It limits the liability of top management and directors, by carefully articulating the decision making process
- It has long term reputational effects among key stakeholders,

Principles of Corporate Governance

- Ethical and disciplined corporate behavior
- Independent and considered judgment
- Parity between accountability and responsibility
- Transparency and effective and adequate disclosures.
- Success of a good governance culture depends upon the perpetual existence and effective and, most important, ethical interplay of these planks not only by themselves, but also with other variables in the social and economic environment (i.e., the stakeholders) of the company

Corporate Governance Reports

- 1992 Sir Adrian Cadbury Committee, UK
- 1994 Mervyn E . King’s Committee , South Africa
- 1995 Greenbury Committee , UK
- 1998 Hampel Committee, UK
- 1999 Blue Ribbon Committee, US

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- 1999 OECD -Organization for Economic Co-operation and development - Principles of Corporate Governance
- 1999 CACG - Common Wealth Association for Corporate Governance - Principles for Corporate Governance in Commonwealth
- 2003 Derek Higgs Committee, UK
- 2003 ASX Corporate Governance Council, Australia

Committees in India

- 1998 CII Code on corporate governance (Desirable Corporate Governance: A Code)
- 1999 Kumar Mangalam Birla Committee
- 2002 Naresh Chandra Committee
- 2003 Shri N. R. Narayana Murthy Committee

Laws governing Corporate Governance in India

- Some aspects of corporate governance have been enshrined in the law that is administered by the Ministry of Corporate Affairs, Securities and Exchange Board of India (SEBI) and other sectoral regulators.
- However, a transparent, ethical and responsible corporate governance framework essentially emanates from the intrinsic will and passion for good governance ingrained in the business entity.

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- The Companies Act, 1956 covers corporate governance widely through its various provisions such as inclusion of directors' responsibility statement in the directors' report under Section 217(2AA), constitution of audit committee under Section 292A fixing maximum ceiling on remuneration that can be drawn by a director under Schedule XIII, and those relating to oppression, mismanagement, etc.
- Further, environmental and other pieces of legislation also protect different stakeholders' interest, ensuring, in the process, good corporate governance.
- The Listing Agreement and Clause 49 of Listing Agreement deals with Corporate Governance norms that a listed entity should follow.

Clause 49 of The Listing Agreement

- The Listing agreement contains 51 clauses and is identical for all Indian stock exchanges.
- The penal provisions for non compliance of the conditions of the Listing Agreement are governed by Sec 23(2) and Sec 23E of the Securities Contracts (Regulation) Act 1956
- The Securities and Exchange Board of India (SEBI) monitors and regulates corporate governance of listed companies in India through Clause 49 of the Listing Agreement.
- This clause deals with Corporate Governance norms that a listed entity should follow

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- Clause 49 was first introduced in the financial year 2000-01 to the Listing Agreement consequent to the recommendations of the Kumarmangalam Birla Committee on Corporate Governance constituted by the Securities Exchange Board of India (SEBI) in 1999.
- Based on the recommendations of Narayana Murthy Committee constituted by SEBI in 2002 to assess the adequacy of current corporate governance practices and to suggest improvements, a modified Clause 49 was issued on October 29, 2004 which came into operation on January 1, 2006.

Clause 49 and Investor Perception

According to FICCI-Grant Thornton “Corporate Governance review of the mid-market listed companies in India” 2010-2011 reveals:

- 84% of the companies feel compliance to Clause 49 and the quality of disclosures have improved the investors’ perception about them
- 24% respondents complied even with the non-mandatory provisions of Clause 49. This is a key positive trend and a significant indicator of developments to come as compliance to non-mandatory provisions not only helps in better corporate governance but makes adoption of these standards easier as and when they get regulatory back up.

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- 90% investors agreed to the importance of corporate governance while making an investment decision.
- 78% of the investors said corporate governance related issues were as important as financial ratios while considering a potential investment
- 89% of the investors felt that quality of information provided by companies was of reasonably good quality and was relied upon by them in making decisions about their investments

Corporate Social Responsibility (CSR)

- CSR - corporate initiative to assess and take responsibility for the company's effects on the environment and impact on social welfare
- The three pillars of CSR are
  - environment,
  - society and
  - commerce

CSR in India

- CSR is still voluntary and it is not mandatory in India.
- The Ministry of Corporate Affairs has issued The National Voluntary Guidelines on Social, Environmental and Economic Responsibilities of Business, 2011 in this regard.
- These guidelines are a refinement over the Corporate Social Responsibility Voluntary Guidelines 2009, released by the Ministry of Corporate Affairs in December 2009. Keeping in view the feedback from stakeholders, it was decided to revise the same with a more comprehensive set of guidelines that encompasses social, environmental and economical responsibilities of business.

CSR - Companies Bill 2011

- Clause 135 of the Companies Bill 2011
- Every company having net worth of Rs. 500 crore or more, or turnover of Rs. 1000 crore or more or a net profit of Rs. 5 crore or more during any financial year shall constitute a Corporate Social Responsibility Committee of the Board consisting of three or more directors, out of which at least one director shall be an independent director.
- 2% of average net profits of the previous three years will have to be spent on corporate social responsibility activities with disclosure to shareholders about the policy adopted in the process, giving reasons on failure of implementation

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- The Corporate Social Responsibility Committee shall formulate and recommend to the Board, a Corporate Social Responsibility Policy which shall indicate the activities to be undertaken by the company as specified in Schedule VII (b) recommend the amount of expenditure to be incurred on the activities referred to in clause (a)
- If the company fails to spend the specified amount on corporate social responsibility activities, the Board shall, in its report made under clause (o) of sub-section (3) of section 134, specify the reasons for not spending the amount

CSR and the Climate Change Mechanism

- Public awareness of the threat of climate change has risen sharply in the last couple of years and an increasing number of businesses, organizations and individuals are looking to minimize their impact on the climate.
- Various National and International treaties for mitigation of climate change
- The United Nations Framework Convention on Climate Change (UNFCCC) - International environmental treaty
- The Kyoto Protocol - International and legally binding agreement. An addition to the UNFCCC treaty.
- The Ministry of Environment and Forests is the nodal agency for climate change issues in India.

Sustainable Development

- Sustainable development is a pattern of resource use that aims to meet human needs while preserving the environment so that these needs can be met not only in the present, but also for future generations.
- Principles of Sustainable Development:
  - Concern for the well-being of future generations;
  - Awareness of the multi-dimensional impacts of any decision (broadly categorized as economic, environmental, social); and,
  - The need for balance among the different dimensions across sectors (e.g. mining, manufacturing, transportation), themes (climate change, community cohesion, natural resource management) and scale (local, regional, national, international).

Sustainability Reporting

- No single, universally accepted definition of Sustainability Reporting.
- It is the practice of measuring, disclosing, and being accountable to internal and external stakeholders for organizational performance towards the goal of sustainable development.
- Used to describe reporting on economic, environmental, and social impacts
- A sustainability report should provide a balanced and reasonable representation of the sustainability performance of a reporting organization – including both positive and negative contributions.

Dimensions of Sustainability Reporting

- Sustainability has three important dimensions for all organizations:
  (a) economic viability,
  (b) social responsibility, and
  (c) environmental responsibility
- A Sustainability Report discloses information on the company's activities across the above 3 dimensions

The Global Reporting Initiative (GRI)

- It is network-based organization that has pioneered the development of the world's most widely used sustainability reporting framework.
- The reporting framework is developed through a consensus-seeking process with participants drawn globally from business, civil society, labor, and professional institutions.
- To help improve sustainability reporting, many organizations have turned to the Global Reporting Initiative (GRI) as the quasi-standard setter for sustainability reporting.

GRI Sustainability Reporting Framework

- GRI's Framework consists of the Sustainability Reporting Guidelines, Sector Supplements, National Annexes, and the Boundary and Technical Protocols.
- The Sustainability Reporting Guidelines are the foundation of GRI's Framework. They feature sustainability disclosures that organizations can adopt flexibly and incrementally, enabling them to be transparent about their performance in key sustainability areas.

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- The G3.1 Sustainability Reporting Guidelines are the latest and most complete version. Launched in 2011, G3.1 completes the content of the G3 Guidelines released in 2006.
- G3.1 features expanded guidance on local community impacts, human rights and gender. While G3-based reports are still accepted, GRI recommends that reporters use G3.1, the most comprehensive reporting guidance available today.
- The fourth generation of Guidelines – G4 – are currently in development and will be launched in May 2013.

Important Websites

For Investor Complaints:

- Ministry of Corporate Affairs

http://mca.gov.in/MCA21/

- Securities and Exchange Board of India

http://investor.sebi.gov.in/complaints%20form/lodge%20index.htm

Important Websites

For Investor Information

- http://www.watchoutinvestors.com/default2a.asp

  Public service website sponsored and aided by Investor Education and Protection Fund (IEPF).
- Investor Education and Protection Fund http://iepf.gov.in/default.asp
- SEBI http://investor.sebi.gov.in/

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- Investor Helpline
  http://www.investorhelpline.in/ih/index.aspx
- Portal for Public Grievances
  http://pgportal.gov.in/

About the Author

- *CA. Rajkumar S Adukia is an eminent business consultant, academician, writer, and speaker. He is the senior partner of Adukia & Associates.*
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- *He started his practice as a Chartered Accountant on 1st July 1983, in the three decades following which he left no stone unturned, be it academic expertise or professional development.*

About the Author

- *He has been coordinating with various Professional Institutions, Associations, Universities, University Grants Commission and other Educational Institutions.*

- *Authored more than 50 books on a vast range of topics including Internal Audit, Bank Audit, SEZ, CARO, PMLA, Anti-dumping, Income Tax Search, Survey and Seizure, IFRS, LLP, Labour Laws, Real estate, ERM, Inbound and Outbound Investments, Green Audit etc.*

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Thank You