



INSPIRE
ACADEMY

CS PROFESSIONAL

ESG **Chapter 7**

**Concept of Governance
in Professional
Driven vs Promoters
Driven Company**



CA Mayur Agarwal

Concept of Governance in Professional Managed Co. & Promoters Driven Co. :-

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Importance of governance in family owned business:-

- ① Business development reaches next level.
- ② Continuity of business across business generation.
- ③ Prevention mechanism against lot of tension - that may arise between family members at a later stage.
- ④ Effective corporate governance measures in order to give competition to other players in the global market.

→ Drawbacks of family owned businesses:-

- ① Key managerial positions in such businesses are held by family members.
 - ② Decision making usually vests with the members of the family.
 - ③ In absence of professionalism, a family business may get frequently weighted down with conflicts.
 - ④ Poor accountability & improper operational control.
 - ⑤ Fails to attract or retain good external talent.
 - ⑥ Family businesses are generally operated with the ethos of 'Family First'.
- ~~It is possible to balance the family~~

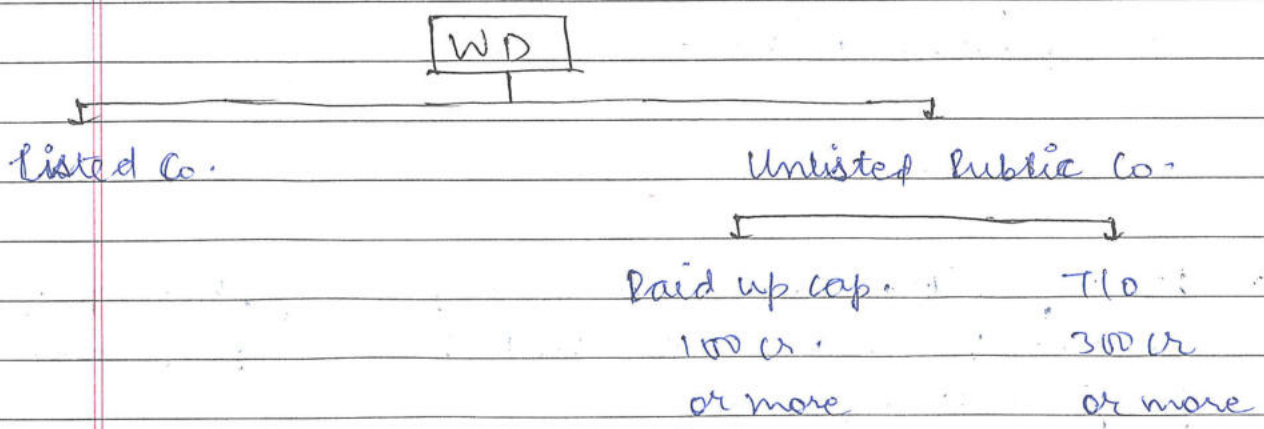
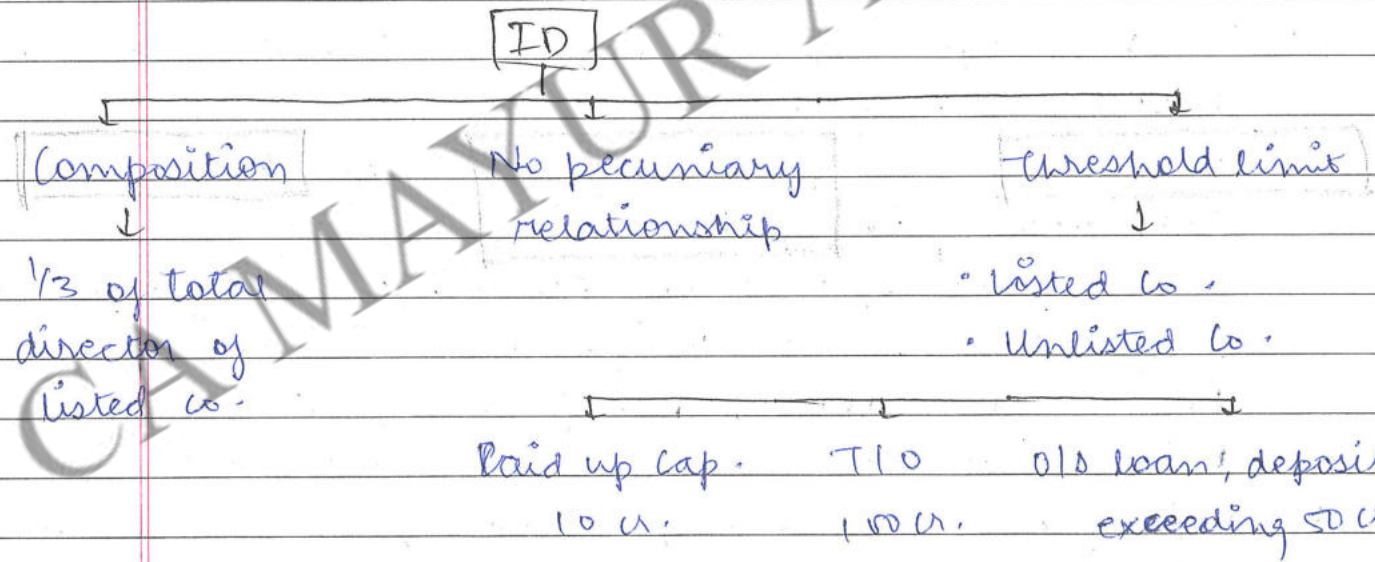
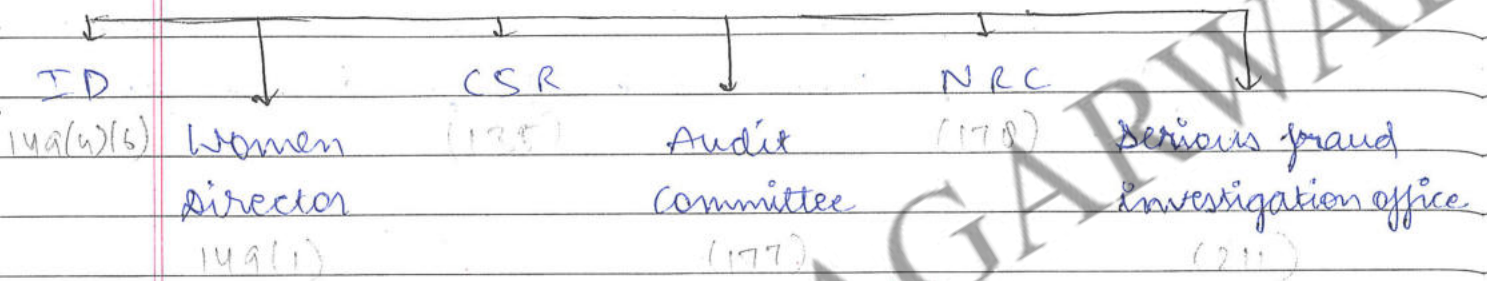
→ Changes observed in family businesses:-

- ① It is possible to balance the family philosophy, culture & personal needs with business performance, profit & transparency.
- ② A visible change can be observed.
- ③ Changing to 'professionally managed' companies.

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- ④ Younger successors have a broad vision & global aspirations.
- ⑤ Prefer working with modern management techniques.
- ⑥ Prefers to create a professional work culture.

→ Provision for Companies Act for family owned businesses :-



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Serious Fraud Investigation office

Formation

Establishment of serious fraud investigation office

Function

look into affairs of the co.
Investigate into incidence of fraud

Receipt of report of registrar or inspector

Public Interest

Request from a department of CA/SA

CSR

Threshold

N.W: 500 cr or more
T/O: 1000 cr or more
NP: 5 cr or more

Composition

Comprising of 3 or more dir. atleast 1 ID

Function

- To formulate policies & recommend activities for promotion of education, equality, etc.
- For social well-being & social publically accountable.

Audit Comm

Composition

Comprising of atleast 3 directors by all listed co. majority have to be ID.

Function

- The member have to be person who have read & understand fin. statement.
- To recommend remuneration & appointment of auditor & reviewing their independence.

NRCComposition

Shall comprise of 3 or more non-ex. directors out of which atleast 50% shall be ID.

Function

- To identify person qualified to become director of co.
- Make recommendation to the board of director regarding appointment & approval.

① ② 2022 Family Business Benchmark: KPMG :-

① Survey → 253,552 family business entities from 11 metropolitan region of germany.

② Factors studied →

- Financial Position
- Cash Flow
- Financial Performance
- Management & Governance Structure.

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③ Facts Revealed :-

- ① Aims for longevity, independence & security.
- ② Hold high proportion of cash.
- ③ Keener to invest.
- ④ Higher equity ratio's in the co.
- ⑤ Own large proportion of fixed asset themselves.
- ⑥ Have greater T/O or more profit.
- ⑦ 74% shares are concentrated in one shareholder or family shareholder.
- ⑧ 70% family business are run by atleast one family shareholder.
- ⑨ Family own business are often run by women (8.7%) as compared to non-family business (7.70%).
- ⑩ All metropolitan area have very high proportion of family owned business.

③ 2021 EY & University of St. Gallen Family Business Index

- ① Basis of report → 500 family owned business according to revenue
- ② Revenue & Employment → Revenue → US \$ 7.20 trillion
Employment → 24.1 million
together they constitute third largest economic contribution in world by revenue.
- ③ Composition of Companies → • Oldest family business on index - Japan's Tatenaka Corporation (business more than 400 years)
• More than half of the ^{german} co's are over 100 years old

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- ④ Board Composition → Total board seats → 4418
 Held by family → 1041
 Proportion → Male → 83%
 → Female → 17%.
- ⑤ Average Age →
- 61 years old (next generation is on its way)
 - One in five business have next generation no. (aged 40 years or younger) on the board.
- ⑥ Shareholding by female family members → 31%.
- ⑦ GRI (Global Reporting Initiative) Reporting → 53% ~~comes~~ (264 Co.'s) reported at least once on GRI database.
- ⑧ Places → 51% comes from EMEA (Europe, Middle East, India, Africa)
 30% → America •
 19% → Asia Pacific •
- ⑨ Contribution by next generation →
- Professional expertise
 - Valuable technology & digital capabilities.
 - Insights into current generation of consumers & employees.

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2022 : Family Owned business survey: Slide :-

- ① To strive for effective governance structure:- There should be effective governance structure to ensure greater harmony among the family members, settle conflicts & create a healthy equilibrium b/w tradition & innovation.
- ② To establish effective conflict resolution Mechanism
Formal family constⁿ, exit & entry provisions & conflict resⁿ mechanism are utmost imp^t. It promotes open & transparent commⁿ & settle conflicts. Regular family meetings are held to align with culture values & vision.
- ③ Succession plan in terms of ownership & management
 - ① Absence of succession plan can lead to power conflicts & are detrimental to the performance of b'ness. ② SP involves engaging the next generation of leaders in decision. ③ The co. must provide leadership development program.
- ④ Many businesses are being managed by non-family members :- Many businesses. Research reveals that more than half businesses being managed by non-family leaders.
 - If business need to be expanded appointment of outsiders as a leader was realised.
 - Non family leader acted as a bridge leader who develop the business & prepare the young family members for leadership roles.
- ⑤ Over 2/3rd respondents have a formal leadership development programme for next generation:- 2/3 respond^t revealed that their orgⁿ has a formal leadership develop^t prog^m. These programs helped families pass on their rich knowledge & heritage to the next generation & motivated them to learn businesses.
- ⑥ ID on board :- Presence of external prof^t helps to explore the benefits of having an outside influence. Many respondent revealed that they have external professionals as the part of the board. 1/5 respondents indicated that they do not external professionals but,

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① India - State of Family Business Report : Centre for family business & entrepreneurship, SP Jain Institute of Management & Research :-

① Background of Survey :- 350 family businesses were surveyed across 50 cities pan-India, out of which 35 were large enterprises, 70 medium enterprises, 140 enterprises and 105 micro enterprises.

② Top Family Challenges (-ve observation) :-

- ① Lack of clear successor / succession plan.
- ② Lack of clearly defined written roles & responsibilities.
- ③ Lack of conflict resolution mechanism.
- ④ Lack of retirement age.
- ⑤ Lack of interest of the next generation.
- ⑥ No unanimously accepted leader.

③ Benefit of family businesses (+ve observation)

Family businesses are governed by clear values & code of conduct.

Way Forward (Contribution to Indian Economy) :-

① 19% of India's GDP :-

③ PWC → Refer Pg. no. 126

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Case studies :-

① Marico Limited - Professionalizing of the board :-

- Name → Marico Limited
- Facts → One of India's leading companies in the fast moving consumer goods (FMCG) & skin care businesses.
- Founder → Harish Marwala.

① Harish Marwala joined his family-owned commodities trading business before eventually founding Marico in 1990.

② Marwala turned the family owned co. into one that is now perceived by the market to be a well managed professionally run co.

③ In 2014 Marwala inducted a professional MD on board - Saugata Gupta.

④ He made his own role & no longer look after the day to day operations instead allowing a team of professional to run the co.

⑤ His son 'Rishab' spent 3 years at Kaya a beauty salon then left to start a venture of his own.

⑥ His daughter 'Pajvi' left the co. & is now a canine behaviorist. His children are no longer part of management or board.

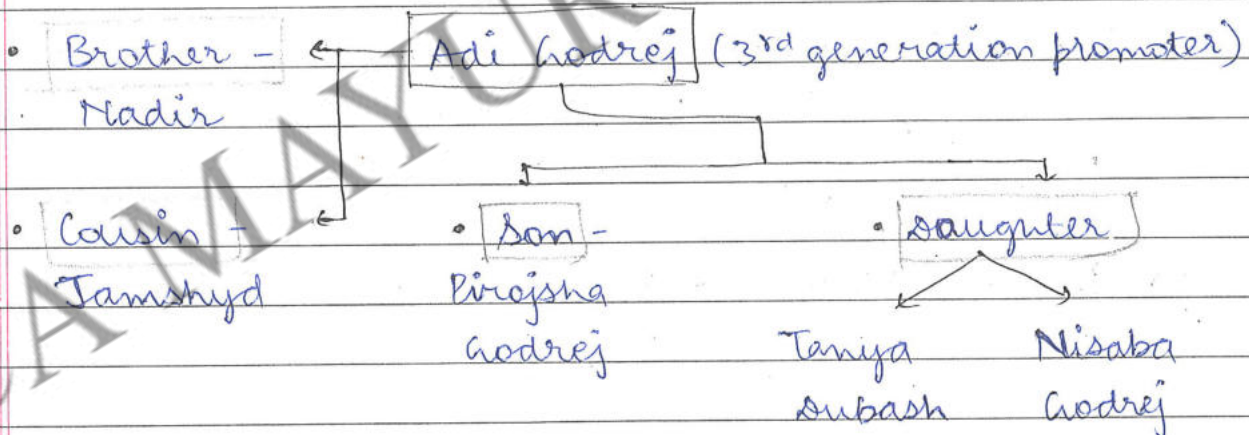
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⑦ Maruwalla stated that he intends to make himself redundant in co. over time making investment in professional leadership & staying away from day to day management.

⑧ Marico is excellent example of the promoters handing over the leadership to a professional & distancing themselves from day to day operation.

(II) Godrej - Clear Responsibilities for next generation promoters

→ Family tree of Godrej



① Large Indian Conglomerate (Consumer products, real estate, consumer durables)

② Godrej co. are run by combo of family members & industry professional.

③ There is facilitator to oversee succession planning.

④ Family members entering business is req^d. to be well qualified.

⑤ Succession plan of Godrej ensures clearly defined roles for next generation based on their strength.

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GODREJ GROUP

Godrej Ind-
-ustries Ltd.

- Chairperson -
Adi Godrej
- MD -
Nadir
- Exec. Director -
Tanya Subash
- (Previous immo?
Strategy leader
- Nisaba Godrej)

Godrej Nature's
Basket

- Chairperson -
Tanya
Subash.

Godrej Agro-
-vet Ltd.

Earlier
Nisaba
was involved
in agri-
-business

Godrej
& Boyce

- Chairperson -
Jamshyd
Godrej

Godrej Consumer
Products Ltd.

- Executive
Chairperson -
Nisaba Godrej
- MD -
Vivek Gambhir
(Professional)

Godrej
Properties

- Since 2012,
• MD + Chairperson -
Poojsha Godrej
- Now, from 2017,
• Executive Chairperson
Poojsha
- MD -
Mohit Malhotra
(Professional)

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(I) Way Forward (Contrⁿ. to Indian Economy & Benefits)

- ① 79% of India's GDP come from family owned-businesses.
- ② Family businesses display conviction & resilience.
- ③ Family businesses should adopt new age technologies.
- ④ They also contribute in growth & stability.
- ⑤ 111 publicly traded family run co. are valued at USD 839 billion.
- ⑥ Family-run businesses generally engage in internal & external collaboration.
- ⑦ Family businesses are rooted in trust, integrity, brotherhood.
- ⑧ 70% of businesses gone out of way to retain their staff.
- ⑨ They do not rely on external entities for capital.
- ⑩ Such businesses are doing quite well.

(II) PWC's Family Business Survey : 2023 :-

- ① Background of Survey :- • Trust is a vital competitive advantage that sets family businesses apart from other countries companies.
 - 2,043 family business owners in 82 territories uses a model developed by Sandra J. Sucher, a Harvard Business School professor of management & the author, with Shikha Gupta, of the Power of Trust, to assess whether family businesses are doing right things to build trust in today's world.

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- ② Four Pillars of Trust :-
- ① Competence → Is the co. good at what it does?
 - ② Motive → Whose interests is the co. serving?
 - ③ Means → Is the co. using fair means to achieve its goals?
 - ④ Impact → What is the tangible impact the co. has, as opposed to the impact it claims to have?

③ Survey regarding trust :- Many businesses are not taking actions that is required to build trust :-

- 59% do not communicate their purpose externally.
- 84% do not take public stance on important issues.
- 85% do not have clear & communicated ESG strategy.
- 79% do not have purpose statement / commitment that advances DEI.

#

Promoter Driven Companies

V/S

Professionally Managed Companies

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	Bharti Airtel	Bajaj Auto	Tata Motors	IITC	HDFC	LLT
Chairperson	Executive Dir. (Non-Promoter)	Executive Dir. (Non-Promoter)	Non-Ex. Dir. (Non-Promoter)	Executive Dir.	Part time Chair & Indep. Dir.	Part time Chair & ID
Separation of role of Chairman	Yes	Yes	-	No	Yes	Yes
Promoter's holding	55.02%	54.98%	45.81%	Nil	25.63%	Nil
Public Holding	44.93%	45.02%	54.19%	100%	74.37%	100%
Date of incorp ⁿ	07/07/1995	30/04/2007	02/09/1945	24/08/1910	30/08/1994	07/02/1946
% of ID	50%	50%	50%	50%	72%	44%
Comp ⁿ of BOD as on 31/3/22	<ul style="list-style-type: none"> 11 Directors 6 ID's (2 WID) 3 Non-Ex. Dir. 1 CP & 1 MD/CEO 	<ul style="list-style-type: none"> 14 Directors 3 Exec. Dir. (incl. MD) 4 Non-Ex. Dir. 7 ID's (incl. 2 WID) 	<ul style="list-style-type: none"> 8 Directors 7 Non-Ex. Dir. 4 ID's (incl. 2 WID) Non-Exec. Chairman 	<ul style="list-style-type: none"> 16 Directors 1 CP 3 Exec. Dir. 0 ID out of which 2 WID 4 Non-Exec. 	-	<ul style="list-style-type: none"> 1 group C.P. MD & CEO 7 Exec. Dir. 1 Non-Ex. Dir. (1 nominee D.) 0 ID

Vision

The Co's vision

Tata has outlined

To achieve susta

Bank has been

Co. committed to

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Vision, Mission, Strategies linked to ESG

The Co.'s vision is to globally renowned environmentally conscious resp^e & Governance led Co. by implementing ESG practices & report.

Tata has outlined sustainability strategy & action plan towards net zero emission for handling the global challenge of climatic change.

To achieve sustainable vision the Co. continues sustainability policies across the orgⁿ.

Bank has been reporting to the Carbon Disclosure Project (CDP). Bank will assess climatic risk in medium term. The parameters like GHG, Air pollution are assessed at sector level & borrower level.

Co. committed to energy transition & sustainability by water neutral by 2035 & carbon neutral by 2040. ESG roadmap is aligned with 5 yrs strategic plan - 'Lakshya' 2026 with a commitment to climate leadership, water stewardship, circular economy, green supply chain, biodiversity & green offering. Opportunities like green hydrogen, clean energy technol. & offshore wind has identified as new growth avenues.

E-mobility & usage of 100% renewable energy will be the key steps towards carbon footprint reduction.

Succession Planning

Succession planning framework is in place. It is placed for top level & senior management. BOD, HR & NRC & Apex talent council responsible for succession planning.

Succession plan is placed before the board for its review. The board of the Co. satisfied itself that plans are in place for orderly succession.

There is leadership succession plan to ensure orderly succession. NRC along with the board works on this plan. The Co. strives to maintain appropriate

The succession planning have helped employees to realise their potential & craft their careers.

NRC & board review the succession plan. The board comprises combination of skills & experience. Succession planning at

Robust process of building talent pipeline helps in succession planning. Development is a place where high performing employees get

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Succession rate is 95%

balance skills & experience

Senior managt. provides business assurance & continuity.

assessed on competencies.

Board level ESG & Sustainability Committee

ESG Commi - ttee

• Provides strategic guidance & decision making on ESG

Safety Health & Sustainability committee

• Review's the Co.'s performance on safety health & sus. aspects

CSR & Sustainability committee

• Review & oversee implementation of sustainability policies

CSR & ESG Committee

• The ESG apex committee oversees sustainability report - ing initiative, climate change disclosures, ensure reduction of overall emissions & track its progress on ESG

CSR & Sustainability Committee

Responsible for sustainability issues -

Business Continuity Plans

Business Continuity & disaster mangt. plan -

• Enabled work from home facility for all the emp^s by providing necessary IT infrastructure

• keeps a close

Business continuity plan

• Disaster managt. plan, designed to address the threat of disruptions to business activities or processes.

Internal Audit Department

Evaluates the quality of Bank's disaster recovery & business continuity plans

Self assessment

• Emergency preparedness plans at each project site to deal with the emergency situations
• In the event of emergency the same shall be investigated and

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renewing infrastructure

- keeps a close watch on compliances with regulations & laws.

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processes

Self assessment of internal financial controls in terms of Sarbanes Oxley Act and Co.'s Act, 2013.

same shall be investigated and appropriate preventive measures would be initiated.

- Relevant infoⁿ & training related to emergency preparedness shall be provided.
- Duties & responsibilities of all workers are being communicated periodically.

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Some Challenges / Governance Issues of Family B'ness:-

- ① Diverse Opinion of family members :- Managing the diverse opinion of family members in business.
- ② May abuse the rights of other shareholders :- Controlling family may abuse the rights of other shareholders, so investors shall scrutinize such co's before investing.
- ③ Multiple leadership position :- Multiple stakeholders for the leadership position.
- ④ Lack of communication :- Between the incumbent & incoming generations.
- ⑤ Succession Challenges :- The incumbent do not know how to handle the succession challenge, while the incoming generation does not know how to raise it.
- ⑥ Sole power of family :- Hiring external staff which may perceive that career advancement, freedom & decision making are solely the purview of family.
- ⑦ No enough attention to process of succession :-
 - Ownership & management succession are the key concerns, they do not devote enough attention to the process involved.
 - Succession dilemma is closely related to the family policy on entry of new generation.
 - Entry of new family member's depends upon 'space' available in the orgⁿ.

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• Younger generation may face difficulties in proving themselves to the former generation.

⑧ Change in mind set :- Differing views b/w the older generation & the newer generation.

⑨ Lack of competitiveness :- • Many Indian co's were family owned, but under competitive pressure for first time.

- Many firms, did not have strategy to respond & took it as threat rather than opportunity.
- Huge tensions in division of assets.