INTERNATIONAL JOURNAL FOR CORPORATE AND COMPETITION LAW [IJCCL]

2025 || ISSN. 3049-3560 (Online) || Volume 1 Issue 3

ISSN: 3049-3560 (O) International Journal for Corporate and Competition Law Vol. 1 Issue 3 (Jun-Aug)
IJCCL

ISSUES OF GOOD GOVERNANCE IN PUBLIC SECTOR BANKS IN INDIA

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INTRODUCTION

Since a few years, public sector banks have been a key player in dominating the banking sector of India and also helping in the growth of the economy of the country. Public sector banks are the banks in which the majority stake is of the government. The stake of the government in these banks are more than 50%. So, these banks are owned and are controlled by the central government. Some examples of these types of banks are State Bank of India, Union Bank of India, Central Bank of India etc. In the last few years, these public sector banks are turning into huge firms or companies and there is a need to implement good corporate governance for the smooth functioning of these banks.

The impact of the global financial crisis has compelled the banking sector worldwide to review and go through their corporate governance practices to help ensure stability of their enterprises and also of public sector banks across India.Though the Indian public sector banks were less affected by the global financial crisis and were protected due to extensive public ownership and rigidity in regulation. It also led to the growth of these banks during this crisis and gained a lot of importance.[2]

Corporate Governance in recent times is one of the most trending and debated topic in India. This has been due to the influence of Globalization. The concept of governance are the processes and the practices which are used by the corporate companies to have a transparency, equity and for the smooth functioning of the activities in their company. These are a combination of laws, policies, customs and processes which determines the way in which the company should be directed and controlled. These are the guidelines which are issued to the top level management such as directors to run their business efficiently.

The proper application of the rules of corporate governance will enable the board and the management in carrying out the goals and interests of the company and the shareholders and

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[2]As mentioned in the India's Bank Nationalization Act, the government secures all the deposits at the public sector banks.

also have a check on the functioning of the company. Milton Friedam has coined the definition of corporate governance for the modern era. In his definition he has stated that the business should be conducted keeping in mind the desires and the goals of the shareholders and the owners whose ultimate aim will be wealth maximisation and earning profits. In modern times other than the shareholders, corporate governance is winning the interests of stakeholders like customers, employees and suppliers. It is also fulfilling the legal and the regulatory requirements which are needed by the companies other than the environmental and communityneeds.The government and the supervisors are also considered as the stakeholders in the company due to the banks having an important significance in the financial system and the local economies.

A good corporate governance structure is essential for the companies to stand out in the competitive world and also helps themin improvingtheir health in the corporate sector.This is helpful in managing the public affairs of the company and serve as a meeting and interacting ground for the citizens of the country and also the shareholders who have invested in the company. This concept also ensures that the day to day activities taking place in the company are according to the expectations of the public and are legal in nature. The activities should also comply with the expectations of the shareholders who have invested in the company.There has not been a practice of good corporate governance in the public sector banks over the years. Issues like demotivated work environment in the companies, red tapes have been common in the recent times.

There is a need to implement banking policies which are effective and this should be the top priority of the banks. To counter these issues faced by the banks, they have developed solutions to these problems such as formation of new committees for new departments like Management Committee, Audit Committee. The banks have also started following the rules which are issued by the Reserve Bank of India. The role of the implementation of the concept of good governance lies in the hands of the top level authorities and the Board of Directors for the growth of the company and progress of the nation.

LITERATURE REVIEW

1. Corporate Governance of Public Sector Banks by Lalita Som[3]

In this research paper, the author has given a brief about the public sector banks in India. The author has also then explained about the governance which takes place in the public sector banks of India. The issues faced by the public sector banks while performing the task of governance to improve the competition, functionality and performance of all public sector banks are also mentioned. Through this article, the researcher has understood the topic really well and got to know more about the public sector banks and the concept of governance in it in detail.

2. Corporate Governance Issues in Banks in India by Dr. R. Seenivasan[4]

In this journal article, the author has mentioned about the importance of governance in public banks and the issues and the priorities while governing. The role of the Reserve Bank of India in the governance of these banks are also included in the journal. With the help of this article, the researcher got aware of the problems faced by the public sector banks while taking into consideration the matter of corporate governance and the steps taken by RBI to solve these issues as it is the banking regulator of Indian banks.

3. Corporate Governance in Banking Sector: A Case Study of State Bank of India by Dr. Srinivasa Rao Chilumuri[5]

In this article, the author has mentioned about the evolution of corporate governance in the banking industry of India.A case study is also done by the authors taking into account the decisions and directives taken by the State Bank of India. The practice of governance followed in State Bank of India is also mentioned. By referring to this article, the researcher got an insight as to how corporate governance takes place in a public sector bank such as State Bank of India and the current status and the importance of corporate governance.

[3]Lalita Som, Corporate Governance of Public Sector Banks, Academia, (Aug 3, 2020,10:30P.M.), https://www.academia.edu/31046023/Corporate_Governance_of_Public_Sector_Banks.
[4]Dr. R. Seenivasan, Corporate Governance Issues in Banks in India, 2 Journal of Business Law and Ethics 91 (2014).
[5]Dr. Srinivasa Rao Chilumuri, Corporate Governance in Banking Sector: A Case Study of State Bank of India, 8 IOSR Journal of Business and Management 15 (2013).

4. Corporate Governance in Indian Banking Sector by Dr. Rana Zehra Masood[6]

In this article, the author has explained the concept of corporate governance in detail. He has also stated the need for this concept in the public banks of India and its role in these banks with the issues which are faced. Through this article, the researcher has clearly understoodand is able to form an overview on the topic of corporate governance and how it is dealt by these banks in current times.

5. Corporate Governance in Indian Banking Sector: An Analysis by Ram Singh and Rohit Bansal[7]

In this journal article, the authors have tried to convey the meaning and the history of corporate governance in depth. They have also cited the role of the RBI in these matters which has helped the researcher in knowing the powers of RBI and the issues which are faced by the public sector banks when they are not in compliance with the standard administrative decisions which are required to be taken by the banks for proper and efficient functioning.

6. Corporate Governance Practices in Public and Private Sector Banks by Rakesh Kumar[8]

The author of this article has listed out several reasons for adopting corporate governance practices in the public sector banks and the need of it in modern times. The author has also focussed on giving a brief about how these practices are applied by these banks to improve their functioning. The author also emphasises on the steps which these banks take to improve these practices in their companies. This article helped the researcher in understanding and forming an insight about the management structure of the banks and also the guidelines which are issued by the RBI to these banks which needs to be followed by the top level management of the banks.

[6]Dr. Rana Zehra Masood, Corporate Governance in Indian Banking Sector, 1 International Journal of 360^{o} Management Review 1 (2013).
[7]Ram Singh and Rohit Bansal, Corporate Governance in Indian Banking Sector: An Analysis, 12 Journal of Xi'an University of Architecture and Technology, 480 (2020).
[8] Rakesh Kumar, Corporate Governance Practices in Public and Private Sector Banks, 2 International Journal for Innovative Research in Multidisciplinary Field 338 (2016).

7. Fixing Governance Problems of Indian Public Sector Banks by N Balasubramanian[9]

In this article, the author has mentioned his views that the government should take to restrict the issues arising from the inadequate corporate governance practices in public sector banks in India. The author has explained his views in context with the Punjab National Bank scam done by Vijay Mallya. The author has also mentioned the steps required for improving these practices in the banks and the initiatives to be taken by the government. Referring to the authors views, the researcher got a professional opinion on this topic and this helped him understand the topic better.

SIGNIFICANCE AND NEED OF CORPORATE GOVERNANCE IN PUBLIC SECTOR BANKS

Significance: -

The main essential factor in any company to determine and improve the bond or relationship of the bank's stakeholders, their Boards and the management level is good corporate governance practices followed by the company.Any conflicting interests among the managers and the Board and the shareholders and the depositors can be resolved by this practice. A good corporate governance practice helps in eliminating the misuse of power in the banks and regulates and keeps in check the behavior of the bank managers. The inefficiency or inability of the Board of the banks to monitor the functioning of the managers often lead to them involving in activities which are of high risk in nature. Therefore, an effective system of corporate governance in the banks will improve the quality of work of the managers and also open the doors of the banks to capitalize on their profit making opportunities in compliance with the interests of the shareholders and the depositors.

Need: -

One of the most crucial factors for the banks to survive in this period of globalization and liberalization is the concept of corporate governance. This concept is required for the banks to stand out in the competitive industry and also have a stable and systematic progress of the banks. Corporate governance enables in carrying out the activities of the banking enterprise

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[9] N Balasubramanian, Fixing Governance Problems of Indian Public Sector Banks, BloombergQuint, (Oct 9, 2020, 10:41 P.M.), https://www.bloombergquint.com/pnb-fraud/fixing-governance-problems-of-indian-public-sector-banks.

which are considered to be fair in the eyes of the stakeholders which comprises of the society, employees, shareholders, bank customers etc. Because of the nature of bank transactions in the banking sector, corporate governance is considered to be very much vital. Banks are responsible for the economic development of the nation and are also considered as the life-blood of the country. It regulates the cash and credit flow and is also in charge of recording the financial transactions of the economy.

It is mandatory for the banks to highlight the corporate governance practices implemented by them in the financial statements of their enterprise. The balance sheet of the company should also be clearly presented to the public and the practices should be in regards to section 49 of the corporate governance rules.[10] Information such as ratios used for accounting, the value of the assets held by the company, advances, investments, borrowings and deposits made by the company.

Only those audit reports of the banks should be revealed to the public which are in compliance with the rules of corporate governance. It is the task of the auditors to be fully aware of the guidelines which are issued by the Reserve Bank of India (RBI) so that the financial statements issued by the company are devoid of any corrupt practices and should reflect the corporate governance practice used by the company. It is important for the banks to also focus on the internal management and functioning of the company so that they are able to maximize their profits on every unit of capital and can develop an effective strategy for funds allocation and management.The company should stick to the goals laid down by them and in accordance run the day-to-day activities of the company.

The objectives of the fir should be in compliance with the interests of the stakeholders and should follow all the laws applicable and the legal procedures. This will help the business function in a smooth and efficient way. As the banking industry is facing a cut throat competition, it has become necessary for the banks to provide its customers those products and services which are in need of the customers. The banks also have the task of completing the recording of the transactions as soon as possible and also to train and improve the skills and knowledge of the employees so that the work can be carried out professionally and there is an element of competition among the employees. It is also important for the banks to capture the attention of the investors as they have a presumption that the company with a

[10] This was stated in the Basel Committee Report, 1999.

good governance policy will reap better returns on their investments and their money invested in the company is in safe hands.

CORPORATE GOVERNANCE IN PUBLIC SECTOR BANKS IN INDIA

A major portion of the Indian banking sector is still dominated by the public sector banks despite the introduction of globalization, privatization and liberalization and it facing competition from private and foreign banks.The major chunk of the ownership is vested in the government as they help in developing and funding the public sector banks and also aid in improving the financial systems. The government also protects the interest of the shareholders. For the banks to function smoothly and efficiently, the Basel Committee has issued out certain guidelines or strategies which the banks have to execute it well.The modern public sector banks are not implementing the principles of corporate governance correctly. These banks have been facing a lot of issues such as bureaucratic hassles, red tapes and the employees surrounded by a demotivated work culture. The banks have been loaded with the role of fulfilling the social responsibility. They are also forced to work and implement those policies which are sanctioned by the ruling political party and because of this the banking policies which are of utmost importance and which are necessary are excluded. The element of monopoly in the public sector banks have protected them from facing immense competition and the bank management have been satisfactory.

The concept of corporate governance in the public sector banks is important not only because they are dominant in the banking industry but also that they are improbablethat they will exit from the industry. Due to the public ownership in the public sector banks, the government will look to fulfil its goals as owners and the intricate role of principal-agent relationship cannot be excluded. The public sector banks are not allowed to follow the private sector banks even though the governance principles are similar.The change in the ownership also results in a disruption in the governance practice as the nature and the character of ownership will also change.The mixed structure of ownership always leads to conflicting interests between both the parties wherein the government focusses on commercial return and the other party has contrasting opinions and objectives.Several other features such as expectations of the banks, risks to its reputation should be included and considered. Corporate governance also provides the management and the Board of the public sector banks the guidelines on which the banks should run their business.

ISSUES FACED BY THE PUBLIC SECTOR BANKS IN CONDUCTING CORPORATE GOVERNANCE

Indian banking system was not affected much by the global financial crisis due to the banks having public ownership. The downfall of the public sector was wrongly interpreted by the public as the strength of these banks during the crisis and was neglected. These banks have been facing a downfall since a long period of time. The performance of these banks were not meeting the highest standards and are considered to be as average. The banks have also been utilizing more resources than needed which leads to the reduction in the capital investment and the economic growth.

- **Legal and Institutional Framework**

The public sector banks have a complex framework. These banks are regulated by numerous authorities such as Bank Nationalization Act, the SBI Act, Banking Regulations Act, Clause 49 of the Listing Agreement, Central Vigilance Commission (CVC) and Central Bureau of Investigation (CBI). The rules followed by the public sector banks is unreal and is difficult to implement in reality, whereas the laws followed by the private banks are strictly in accordance to the rules of corporate governance.For the banks to function smoothly, the RBI has to provide them with circulars and notifications which consists of matters relating to governance and carrying out operations. This slows down the decision -making capacity of the banks and is rather ineffective and tedious. Therefore, there should be a common legal framework for all the banks so as to keep the banks on the same level, the public sector banks can focus more on the outcomes of their decisions, the true facts can be displayed to the public and avoid any fraudulent activities in the market and make it impossible for the supervisors to interrupt in the normal functioning of the business.

- **Micro Management by the RBI**

With the RBI also involved in the decision- making process of the public sector banks, this has taken away the right of the banks to take their own decisions independently and it also creates a sort of confusion in the chain of command for corporate governance as they are in doubt as to whose orders to follow. The spoon feeding from RBI has rendered the public sector banks inefficient to function independently as they are very much relied on the apex bank and are unable to form their own strategies.This ultimately leads to lazy banking by the

Board and management members and they do not perform their duties in true spirit of banking needs.

- **Non-performing Assets**

The main issue which the public sector banks are facing is the non-performing assets. This problem has risen due to these banks involving in huge risky infrastructure projects which are taken up by the government. Often the public sector banks are targeted by the fraudsters who bribe the employees or get their work done by some influence of dominant personalities of political parties.These fraudsters take loan from one public sector bank and also from another for different businesses and fool them by showing the same shares as collateral for the loan. The idea is to repay the loan of the first bank with the amount taken by the other bank which means that the other bank is repaying the loan given by the first bank. This is strictly in violation of the rules of RBI and is considered as fraud. The banks in return have to raise the amount of interest in order to recover the value of bad debts. For instance, the Rs 9000 crore scam done by Vijay Mallya by borrowing money from different public sector banks and refusing to pay it when asked to repay. He had bribed the employees who gave him the loan and got it without showing any documents.

- **Risk Management**

The banks in order to improve their profitability margin and to manage their capital more resourcefully, in recent years have started to develop and strengthen their risk management systems and adopting and implementing advanced approaches. The risks to the business should be effectively managed by the Board and the management to increase the ability of the business to fight back against risks. The credit accessing power of the public sector banks and the monitoring systems are relatively weaker in these types of banks.The corporations which have taken loan from the public sector banks tend to be irresponsible in repaying the loan and this shakes the trust of the public from the banking system. The bank monitoring systems and the credit appraisal bodies are not given the ultimate authority to control the funds and keep a check on the origin of the funds and also prevent them from being diverted.

- **Minority Shareholders**

The government considers itself as the sole decision maker in the public sector banks and neglects the shareholders who have a minority stake in the business. There is a limit on the rights of the shareholders in the public sector banks and their voting rights are restricted to 10 percent. The Ministry of Finance has issued advisory notices to the public sector banks to present their plans to the Board and the management and bring it to execution in a short span of time. The minority shareholders are not allowed to express their opinion on this matter even though they do not support the plans laid down by the banks. They are deprived of taking decisions on matters like approving dividends, viewing of annual reports of the company, making comments on the structure or the number of members in the Board and also not able to select the statutory auditors. Though the minority shareholders have some rights enshrined with them, the majority part is dominated by the government.

ROLE OF SEBI AND RBI IN GOVERNING CORPORATE GOVERNANCE IN THESE BANKS

The Reserve Bank of India plays a very important role in the public sector banks not only in monitoring that the principles of governance used by the banks but also keeping a check on the bank's Board so that they perform their duties diligently and without any fraudulent activity being conducted. The RBI has the authority to go through the minutes of the meetings of the Board, ensuring that the employees are granted with access to important information, going through the meetings of the Board whenever they are deemed to be necessary, they also can issue warnings and also compel the Board to reconstitute its framework so that the corporate governance principles are applied in accordance and effectively. The private sector banks and the public sector banks are given equal preference in the matters which require reasonable care. However, the public sector banks are excluded from some of the provisions of the Banking Regulation Act even though they are under the territory of matters which require care and attention. For these matters the RBI formulates certain rules for the private sector banks which are also for the public sector banks which the Government has to implement in these banks.

The RBI in accordance with Securities and Exchange Board of India (SEBI) formulates the rules for the banks according to which the Board has to form their own codes of corporate governance. Often various incentives are also provided to these banks in order to improve their practices of corporate governance. For example, rating mechanisms to determine the effectiveness of the principles of corporate governance can be implemented wherein the RBI can check the factors of corporate governance which are responsible for low rating of the banks and try to implement more profitable measures.For the banks to reconstitute their structure, the RBI should announce their incentives in advance and should be conveyed in a clear and appropriate manner.

The SEBI's Committee for Corporate Governance in its circular dated 21st February, 2000 had issued guidelines for the public sector banks for corporate governance. Some of the recommendations were as follows: -

- The Board of the company should establish an audit committee which is independent in nature and is highly skilled and competent.
- In a year, the audit committee has to necessarily meet thrice. One meeting should be before the company finalizes the audit reports and accounts. One meeting should be held in every six months.
- The minimum number of directors required in the Board should be two and the committee can consist of at least two members or one third members of the audit committee whichever is deemed to be higher.
- The audit committee can put its power into force only if it is permitted by the Board. The powers include investigation of any activity which is under its jurisdiction, if any information is required on any particular employee and if any legal or professional advice is to be seeked.
- It is suggested by the Committee to form a renumeration committee by the Board so that the policy of the company on various renumeration packages for executive directors can be reviewed which includes pension rights and payment of compensation.
- The Committee suggests that the meetings of the Board should be conducted four times a year and the maximum gap between the meetings should be four months.
- It is recommended by the Committee that a director of a company should not hold the position of a member in more than 10 companies or hold the position of Chairman in more than 5 companies. It is advised that the director informs the Board about his position which he is holding in other companies beforehand.

- If the company is planning to disclose its ideas of management, the discussions which were held in the management meetings and the Analysis Report should also be disclosed in the annual reports of the company to the shareholders.
- The Committee suggests that all disclosures which are made by the Management which is in terms for their personal interest and does not meet the goals of the company should be discussed and conveyed to the Board.

CONCLUSIONS/RECOMMENDATIONS

The concept of Globalization and liberalization has not only affected the banking sector but most of the industries of the economy. The modern period is subjected to a lot of changes taking place frequently and it has now become necessary for the banks to resolve all the issues faced by them and minimize the risks which they are foreseeing in future. During this period of cut-throat competition in the banking industry, the company which follows a good corporate governance practice will be able to hold their ground in the market and also will have the opportunity for growths in future. The public sector banks needs to be given the authority to form their own decisions and the RBI should not interfere much in the decision making process of the Board of the company. The banks should recognize their objectives and implement the best possible corporate governance practices to progress and reach success. For reaching the goal established by the banks, they have to follow and implement the rules which are ethical and fair to the society and devoid of fraudulent activities. By fixing the standards of the matters which require care and attention by the companies, it will be able to solve their issues of corporate governance. The RBI has been very much active in the matter since the past few years and has been implementing a lot of new policies for the betterment of the banking industry. In the future, not only will the banking sector grow in its size but also the structures of the management of the banks will also become complex. It is important that the country's financial system and the payment system should be efficiently managed by the RBI. The global financial crisis did not have a direct impact on the banking industry but the banks had to face reduction in the trade and investment flows which slowed down the growth of the industry in the fields of employment generation, poverty reduction and the development of human growth. It is the need of the hour to fix and strengthen the rules and practices of corporate governance for the betterment of the economy of the country as well as the banks.