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"The future of governance: Asia's fork in the road"

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Finding Measurability of Quality of Governance

An Index Provider's Perspective

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Governance parameters



Size of the board and percentage of independence on board



Presence of a non-executive chairperson



Gender diversity



Mandatory board-level committees' composition



Number of board and committee meetings



Attendance in board meetings and mandatory committee meetings



Attendance in annual general meetings



Compensation to non-executive directors



Compensation to executive directors



Statutory auditor's opinion



Secretarial auditor's opinion



Engagement of statutory auditor's for providing non-audit services



Track record of disclosures and regulatory compliance



Direct access to chairperson of audit committee in whistleblower mechanism

Financial parameters



Return on equity



Financial leverage



Earnings variability

Corporate Governance Individual Factor Ratings (1/3)

Sr. No.	Parameter	Sub-Parameter	Ratings	
			Rating of 0	Rating of non- 0
1	Board composition	Size of the Board	As per law and regulations - 0	Non-compliance as per law and regulations - 0.5
		Presence of a non-executive Chairperson	Presence of Non-Executive Chair – 0	Presence of Executive Chair - 0.5
2	Percentage of Independent Directors on the Board		As per law and regulations - 0	Non-compliance as per law and regulations - 1
3	Gender diversity at the Board level		Presence of at least one Woman Independent Director – 0	No Woman Independent Director - 1
4	Composition of mandatory Board-level committees	Audit Committee, Nomination and Remuneration Committee, Stakeholders Relationship Committee, Risk Management Committee and Corporate Social Responsibility Committee	As per law and regulations - 0	Non-compliance as per law and regulations - 0.2 (1/5) 0.25 (1/4) upto FY 19
5	Number of Board and committee meetings	Board, 5 mandatory committees and separate meetings of Independent Directors	As per law and regulations - 0	Non-compliance as per law and regulations - 1
6	Attendance in Board and committee meetings	Attended versus attendable meetings for all Directors taken together (meetings include Board and 5 mandatory committees)	75% or more attendance - 0	Less than 75% attendance - 1 Additionally, if 2 or more Directors have less than 50% - 0.5 If any Committee attendance is not given - 0.5

Corporate Governance Individual Factor Ratings (2/3)

Sr. No.	Parameter	Sub-Parameter	Ratings	
			Rating of 0	Rating of non- 0
7	Attendance in Annual General Meetings	Attendance on the date of AGM, and presence of Chairs of Audit Committee and Stakeholders Relationship Committee	At least 75% attendance of all Directors, including Presence of Chairs of Audit Committee and Stakeholders Relationship Committee - 0	Either condition not fulfilled - 0.5
		Time between date of AGM and date of auditor's report	Up to 60 days - 0	More than 60 days - 0.5
8	Compensation to Non-Executive Directors	Payment of sitting fees	Payment - 0	Non-payment - 0.5
		Payment of profit linked commission	Payment - 0	Non-payment - 0.5
9	Compensation to Executive Directors	Payment of variable pay/ commission	Payment - 0	Non-payment - 0.5
		Provision of stock options	Provision - 0	Non provision - 0.5
10	Statutory Auditor's opinion		Clean report - 0	Emphasis of Matter - 0.5 Qualification - 1
11	Secretarial Auditor's opinion	Secretarial Auditor's report	Clean report - 0	Not clean - 0.5
		Secretarial Compliance Report	Clean report - 0	Not clean/ Fines/ Repeat offence - 0.5

Sr. No.	Parameter	Sub-Parameter	Ratings	
			Rating of 0	Rating of non- 0
12	Engagement of Statutory Auditors for providing non-audit services	Non-audit fee should not exceed 50% of the audit fee paid	Upto 50% - 0	More than 50% - 1
13	Public disclosures	Stock Exchange filings	No disclosure with content inconsistent with Corporate Governance - 0	Any single disclosure with content inconsistent with Corporate Governance - 0.5
		Mandatory website disclosures	All mandatory disclosures on the website - 0	Any single mandatory disclosure not on the website - 0.5
14	Access to Chairperson of Audit Committee in whistle-blower mechanism		Direct access to Chair of Audit Committee - 0	Access to Chair of Audit Committee through common email id or address - 0.5 No details/ access - 1

Step 1: Rating the individual companies on 14 Corporate Governance parameters:

- Companies are rated on each parameter of Governance on a scale of 0 to 1, with 0 representing a perfect rating, and higher than 0 rating representing an inadequacy in regard to the relevant corporate governance parameter. The ratings are based on information in publicly available documents & company filings and are prepared by a team of analysts who are experts in corporate governance issues.
- A rating on a scale of 0 and 1 is assigned in respect of each of the 14 parameters.
- As the rating is done on an inverse scale, sum of scores is to be treated as lower the better.

Step 2: Calculate the Governance Score for each company:

- **Governance Score** = Governance Value * Positive Factor

Where:

- **Governance Value** = $1 - (\text{Sum of scores under each of 14 parameters}/14)$
- **Positive Factor** = 20% reward for companies which achieve all the positive factors.

Step 3: Smoothing of G-Score using exponential moving average of past scores.

- For the first quarter, compute G-scores for last 4 quarters
- For the first quarter, compute the final (Adjusted) G-Score by assigning 50% to the latest score and the rest 50% to the simple average of the scores for the previous 3 quarters.
- Subsequently in next quarters, Governance Score = $50\% (\text{Latest Unadjusted Governance Score}) + 50\% (\text{Previous Adjusted Governance Score})$

The methodology gives greater importance to performance on some Governance parameters, which represent best practices in Corporate Governance. These factors are called 'positive factors' A perfect score on these factors gives a certain boost to the company's overall G score.

Notes on positive factors:

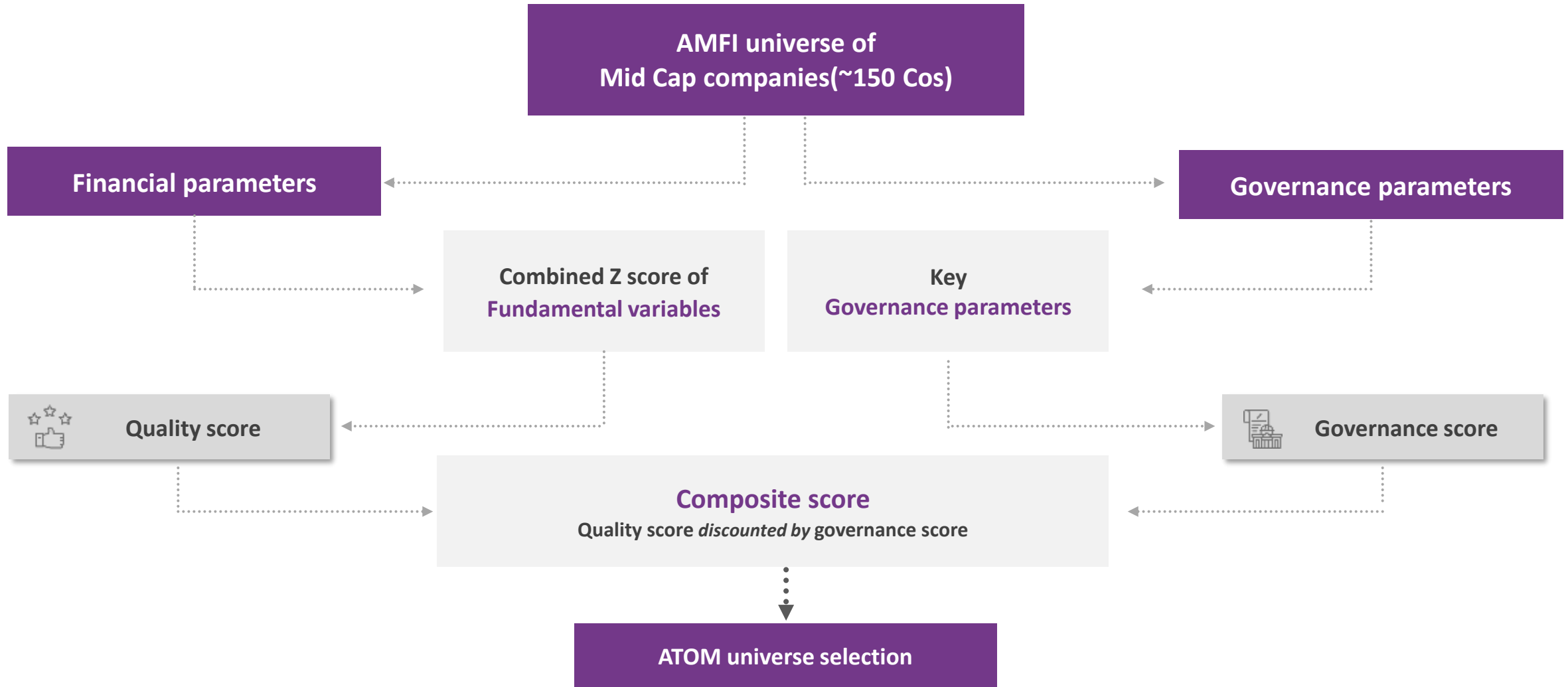
- Presence of 2 or more women Independent Directors
- An Audit Committee comprising only Independent Directors
- 75% or more attendance in the Board and Committee meeting
- Statutory Auditor's opinion
- Engagement of Statutory Auditors for providing non-audit services
- 6 or more Board meetings and 6 or more Audit Committee meetings (in addition to complying with minimum number of meetings for other committees and separate meetings of Independent Directors)

Positive Factor = 20% reward for companies which achieve all the positive factors.

Correlation Between Top Financial Scorer Companies and their Rank in Governance and vice versa

Company Name	Ranking Based On Financial Quality Score	Ranking Based On Governance Score
Colgate Palmolive (India) Ltd.	1	39
Tata Elxsi Ltd.	2	27
Procter & Gamble Hygiene & Health Care Ltd.	3	84
Abbott India Ltd.	4	69
CRISIL Ltd.	5	6
Motherson Sumi Wiring India Ltd.	6	49
Oracle Financial Services Software Ltd.	7	91
KPIT Technologies Ltd.	8	7
Vedant Fashions Ltd.	9	95
CG Power and Industrial Solutions Ltd.	10	120
L&T Technology Services Ltd.	11	25
HDFC Asset Management Company Ltd.	12	82
SKF India Ltd.	13	63
NMDC Ltd.	14	148
Cummins India Ltd.	15	65
Persistent Systems Ltd.	16	107
Grindwell Norton Ltd.	17	74
Coromandel International Ltd.	18	5
Bayer Cropscience Ltd.	19	99
3M India Ltd.	20	40

Company Name	Ranking Based On Financial Quality Score	Ranking Based On Governance Score
Pfizer Ltd.	47	1
JSW Energy Ltd.	140	2
Syngene International Ltd.	55	3
Relaxo Footwears Ltd.	74	4
Coromandel International Ltd.	18	5
CRISIL Ltd.	5	6
KPIT Technologies Ltd.	8	7
Polycab India Ltd.	36	8
Whirlpool of India Ltd.	103	9
AU Small Finance Bank Ltd.	28	10
Oberoi Realty Ltd.	105	11
Tata Chemicals Ltd.	133	12
Schaeffler India Ltd.	21	13
Voltas Ltd.	106	14
Jubilant Foodworks Ltd.	90	15
Indian Hotels Co. Ltd.	107	16
Solar Industries India Ltd.	30	17
Aditya Birla Fashion and Retail Ltd.	149	18
Godrej Properties Ltd.	125	19
Alkem Laboratories Ltd.	77	20



Note: ATOM Index stocks are reviewed four times in a year

Definition of Mid Cap Companies in different Countries



US

Companies with a market capitalization between \$2 billion and \$10 billion.



UK

Companies with a market capitalization between \$600 million and \$2.4 billion.



Australia

Companies with a market capitalization between \$1.25 Billion and \$6.37 billion.



Singapore

Companies with a market capitalization between \$219 million and \$1.4 billion.



Honkong

Companies with a market capitalization between \$640 million and \$5.1 billion.



India

AMFI/SEBI classifies the first 100 companies, by average six-month market cap, as Large Caps, the next 150 as Mid-Caps.

Usually, companies with a market capitalization between \$600 Million and \$2.4 Billion.

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