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# C ORPORATE GOVERNANCE AND FRAUD PREVENTION IN INDIAN COMPANIES

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## I. ABSTRACT

*Corporate governance constitutes the foundational framework through which companies are directed, managed, and controlled. It ensures that business operations are conducted in a fair, transparent, accountable, and responsible manner, thereby safeguarding the interests of shareholders, employees, creditors, customers, and the public at large. In India, the significance of corporate governance has increased substantially in the aftermath of major corporate scandals such as the Satyam Computer Services fraud, the IL&FS crisis, the Punjab National Bank fraud, and governance concerns involving financial institutions such as Yes Bank. These incidents exposed serious deficiencies in board oversight, auditing practices, disclosure standards, and internal control systems. Corporate fraud poses a significant threat to economic stability, investor confidence, and market integrity. It may take various forms, including financial statement manipulation, bribery, corruption, insider trading, money laundering, and diversion of corporate funds. Effective corporate governance plays a crucial role in preventing such misconduct through mechanisms such as independent directors, audit committees, whistle-blower protections, internal audits, and robust disclosure requirements. This research paper examines the relationship between corporate governance and fraud prevention in Indian companies, with particular reference to the Companies Act, 2013 and the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015. It analyses how governance failures contribute to fraudulent practices and evaluates the effectiveness of the existing regulatory framework. The study concludes that although India has made substantial progress in strengthening corporate governance, stricter enforcement,*

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*ethical leadership, and technology-driven fraud detection systems remain essential for ensuring long-term corporate accountability and sustainable growth.*

## II. KEYWORDS

Corporate Governance, Fraud Prevention, Companies Act 2013, SEBI LODR, Audit Committee.

## III. INTRODUCTION

Corporate governance is one of the most important aspects of modern business. In today's global economy, companies are not only expected to earn profits but also expected to operate ethically and responsibly. Corporate governance plays a key role in maintaining trust between the company and its stakeholders such as shareholders, employees, customers, creditors, and government authorities.

In simple words, corporate governance refers to the rules, regulations, and processes that control how a company functions. It ensures that companies are managed properly and do not misuse their power. It also ensures that decision-making is fair and transparent. Corporate governance acts as a protective shield against mismanagement and fraud.

Fraud in companies is a serious issue. Corporate fraud means wrongful acts done intentionally to gain unfair advantage or financial benefit. Fraud is not just a loss for a company; it affects the whole economy. It can lead to job losses, investor losses, fall in market confidence, and loss of foreign investment.

India has seen many fraud cases in the last few decades. The most famous one is the Satyam scam, which shocked the Indian corporate world. It exposed the weakness in board functioning, auditing system, and disclosure requirements. Such frauds forced the government and regulators to strengthen corporate governance laws.

The Companies Act 2013 is a major reform that introduced strict provisions for independent directors, audit committees, CSR, whistle-blower mechanisms, and fraud

reporting. SEBI has also made strong rules for listed companies through SEBI LODR Regulations, 2015.

This paper aims to understand how corporate governance helps in preventing fraud in Indian companies. It also analyses whether Indian corporate governance standards are effective enough or still need improvement.

### **A. Research Objectives**

The present study is undertaken with the following specific objectives:

1. To examine the concept, principles, and significance of corporate governance in the context of Indian companies.
2. To analyse the legal and regulatory framework governing corporate governance under the Companies Act, 2013 and the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015.
3. To study the relationship between governance failures and the occurrence of corporate fraud in India.
4. To evaluate the effectiveness of existing fraud prevention mechanisms, including independent directors, audit committees, internal controls, and whistle-blower mechanisms.
5. To assess the challenges faced in the implementation of corporate governance standards and suggest measures for strengthening fraud prevention in Indian companies.

### **B. Research Questions**

The present study is guided by the following research questions:

1. Whether the existing legal and regulatory framework under the Companies Act, 2013 and the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 provides adequate mechanisms for preventing corporate fraud in Indian companies?

2. What are the principal corporate governance failures that enable fraud, financial mismanagement, and unethical practices in Indian companies?
3. How effective are governance mechanisms such as independent directors, audit committees, internal controls, and whistle-blower mechanisms in detecting and preventing corporate fraud?
4. What are the major challenges in the practical implementation and enforcement of corporate governance standards in India?
5. What reforms and best practices can further strengthen corporate governance and fraud prevention in Indian companies?

### C. Research Methodology

This research paper is based on descriptive and analytical research methodology. The study mainly relies on secondary sources of information to understand the role of corporate governance in preventing fraud in Indian companies. The descriptive approach helps in explaining the concepts and background, while the analytical approach helps in evaluating governance mechanisms, legal provisions, and real fraud cases.

1. **Nature of Research:** The research is qualitative in nature. It focuses on understanding corporate governance principles, fraud prevention mechanisms, and the legal framework in India. The study also analyses how weak governance practices lead to corporate fraud and financial irregularities.
2. **Sources of Data:** The study is based on secondary data, collected from various reliable sources. These sources include:
  - Books related to corporate governance and corporate fraud.
  - Research journals, articles, and published papers.
  - Provisions of the Companies Act, 2013.
  - SEBI regulations and guidelines, especially SEBI (LODR) Regulations.
  - Reports and publications of ICAI, RBI, and SEBI
  - Case studies of major frauds such as Satyam Scam, IL&FS crisis, Nirav Modi-PNB fraud, and other reported corporate scandals.

### 3. Limitations of Study:

- No primary survey or interview has been conducted.
- Study is based on publicly available data.
- Fraud cases are limited to major reported cases only.

## IV. HISTORICAL BACKGROUND OF CORPORATE GOVERNANCE IN INDIA

Corporate governance in India did not develop overnight. It evolved slowly with time. Earlier, Indian companies were mostly family-owned and promoter-controlled. The decision-making was mostly in the hands of promoters and there was less focus on transparency.

1. **Corporate Governance Before Liberalization:** Before 1991, Indian economy was highly regulated. Most industries require government approvals. There was limited competition, and corporate governance was not treated as a major issue. Many companies worked without strong shareholder protection.
2. **Post Liberalization Era (After 1991):** After economic liberalization in 1991, India opened its market to foreign investment. This increased competition and brought the need for better governance standards. Foreign investors wanted transparency, proper accounting practices, and fair management.
3. **Clause 49 and Corporate Governance Reforms:** In the year 2000, SEBI introduced Clause 49 under the listing agreement. This was considered one of the most important reforms in the history of corporate governance in India. The main aim of Clause 49 was to improve transparency and strengthen the corporate governance structure of listed companies. Clause 49 mainly focuses on important aspects such as:
  - Appointment of independent directors to ensure unbiased decision-making.
  - Formation of audit committees to monitor financial reporting.
4. **Satyam Scam and Its Impact:** The Satyam Computer Services scam (2009) was one of the biggest corporate frauds in India. This scam clearly exposed major

weaknesses in the corporate governance system. The chairman of the company admitted that the financial statements were manipulated and profits were falsely increased. This fraud became possible due to several governance failures such as:

- The Board of Directors failed to properly monitor the company's management.
- The auditors failed to identify financial manipulation and fake records.
- The company had weak internal control systems.
- There was a serious lack of transparency and accountability.
- After the Satyam scam, it became clear that corporate governance rules in India needed to be stricter, and their implementation needed to be stronger.

5. **Companies Act, 2013:** The Companies Act 2013 was introduced as a modern and improved corporate law framework. It replaced the old Companies Act, 1956 and brought major reforms to strengthen corporate governance in India. This Act introduced several important provisions, such as:

- Stronger duties and responsibilities for directors and management.
- Mandatory Corporate Social Responsibility (CSR) provisions for eligible companies.
- Compulsory formation of audit committees in certain companies.
- Introduction of class action suits, allowing shareholders to take legal action against wrongdoing.
- Strict provisions related to fraud reporting and punishment.
- Mandatory internal audit requirements for better monitoring and control.
- The Companies Act 2013 is considered a major reform because it focused on improving transparency, accountability, and protection of stakeholders in Indian companies.

## V. LANDMARK CASES IN CORPORATE GOVERNANCE AND FRAUD

1. **SEBI v. Satyam Computer Services Ltd. (2009):** It was held that Satyam Computer Services Ltd. and its management were involved in serious financial statement

manipulation and fraudulent misrepresentation. The company violated disclosure norms and misled investors by presenting false financial records. SEBI took strict action against the company and its officials, and proceedings were initiated to ensure punishment and investor protection.

2. **Union of India v. IL&FS (2018):** It was held that IL&FS was suffering from serious mismanagement and governance failure, which resulted in large-scale defaults and financial instability. The tribunal accepted government intervention in public interest and allowed restructuring of the board and management. The purpose was to protect investors, creditors, and the overall financial system from collapse.
3. **State Bank of India & Ors. v. Kingfisher Airlines Ltd. & Ors., (2017) 6 SCC 654:** The Supreme Court upheld interim directions requiring disclosure of assets and affirmed the authority of lending banks to pursue legal remedies for recovery of substantial outstanding dues owed by Kingfisher Airlines Limited and its guarantors. The case underscored that companies, promoters, and personal guarantors may be held accountable for diversion and misuse of borrowed funds and may be compelled to disclose assets to facilitate enforcement proceedings. It may be noted that separate contempt proceedings were subsequently initiated against Dr. Vijay Mallya for violation of the Court's asset-disclosure orders.
4. **Tata Consultancy Services Ltd. V. Cyrus Investments Pvt. Ltd. (2021):** The Supreme Court held that Tata Sons was not guilty of oppression and mismanagement. The removal of Cyrus Mistry was held to be valid and lawful, and the decision of the board and majority shareholders was upheld. The Court emphasized that corporate decisions taken according to company law and Articles of Association cannot be treated as oppression.

## VI. CORPORATE GOVERNANCE AND ITS IMPORTANCE

Corporate governance is very important for the smooth and proper functioning of a company. It ensures that the company operates in an honest, fair, and disciplined manner. Corporate governance acts as a guiding system that controls how a company is

managed and how decisions are taken. It also makes sure that the management does not misuse its power or company resources for personal benefit.

In today's corporate environment, the importance of corporate governance has increased significantly because weak governance often leads to fraud, corruption, and financial mismanagement. A company with strong corporate governance is more trusted by investors and stakeholders, and it also helps in maintaining the long-term stability and reputation of the organization.

### **A. Meaning of Corporate Governance**

Corporate governance refers to the system through which a company is directed, managed, and controlled. It includes the rules, policies, and procedures that define how the company's management works and how responsibilities are divided among directors, executives, and other stakeholders.

In simple terms, corporate governance ensures that the company's leadership works responsibly and does not misuse its authority. It also ensures that decisions are taken in the interest of shareholders and other stakeholders, and not for personal gain.

### **B. Principles of Corporate Governance**

Corporate governance is based on certain key principles that help a company function in a transparent and ethical manner. These principles are essential for building trust and preventing fraud within organizations.

- 1. Transparency:** Transparency means that the company should openly share accurate and clear information related to its financial position, performance, and major decisions. Proper disclosure reduces the chances of manipulation and helps stakeholders make informed decisions.
- 2. Accountability:** Accountability means that the management and directors of the company must be answerable for their actions and decisions. If any wrongdoing or failure occurs, they should take responsibility and be accountable to shareholders and regulatory authorities.

3. **Fairness:** Fairness means that the company should treat all stakeholders equally. Whether it is shareholders, employees, customers, or creditors, the company should not show bias or provide unfair advantage to any particular group.
4. **Responsibility:** Responsibility refers to the duty of the company to follow laws, maintain ethical conduct, and act in a socially responsible manner. A company should not only focus on earning profits but should also ensure that it operates within legal and moral boundaries.

## VII. CORPORATE FRAUD IN INDIAN COMPANIES

Corporate fraud is one of the most serious challenges faced by companies today. It not only causes financial loss to the organization but also damages its reputation and reduces public trust. In India, corporate fraud has become a major issue because many companies still struggle with weak internal controls, lack of transparency, and unethical practices. Fraud can take place at any level of management, and in many cases, it remains hidden for a long time before being detected.

Corporate fraud affects not only the company but also investors, employees, customers, banks, and even the economy. Therefore, preventing fraud has become an important responsibility of corporate governance.

### A. Meaning of Corporate Fraud

Corporate fraud refers to illegal or dishonest activities carried out by company officials, employees, or management with the intention of gaining personal benefit or misleading stakeholders. These acts are usually planned and intentional, and they are done to hide the true financial condition of the company or to steal company resources.

In simple words, corporate fraud happens when someone inside the company misuses their position or authority to cheat the company or its stakeholders for personal advantage.

## B. Types of Corporate Fraud

Corporate fraud can take many forms depending on the nature of the business and the intention of the fraudster. Some of the common types of corporate fraud in Indian companies are as follows:

- 1. Financial Statement Fraud:** This type of fraud occurs when a company manipulates its financial records to present a false picture of its financial performance. It may include showing fake profits, hiding losses, inflating revenue, or reducing liabilities. The main purpose is to mislead investors, shareholders, and regulators.
- 2. Asset Misappropriation:** Asset misappropriation refers to the theft or misuse of company assets by employees or officials. It may involve stealing cash, misusing company property, inventory theft, or creating fake vendor bills and payments.
- 3. Corruption:** Corruption includes unethical practices such as bribery, favoritism, illegal commissions, and misuse of power. In many cases, company officials may accept bribes to approve contracts, issue licenses, or provide business advantages to certain individuals or firms.
- 4. Insider Trading:** Insider trading happens when company insiders such as directors, executives, or employees use confidential information that is not available to the public to buy or sell shares. This gives them an unfair advantage and harms the interests of other investors.
- 5. Loan and Banking Fraud:** Loan and banking fraud occurs when companies take loans from banks and then misuse or divert the borrowed money for personal gain or other illegal purposes. In some cases, companies intentionally avoid repayment, leading to heavy losses for banks and increasing non-performing assets (NPAs).
- 6. Related Party Transaction Fraud:** This type of fraud takes place when promoters or company management transfer company funds or assets to their

own personal businesses or related companies. Such transactions are often done secretly or shown as legal business deals, but the actual purpose is to divert money for personal benefit.

### **VIII. ROLE OF THE SERIOUS FRAUD INVESTIGATION OFFICE (SFIO) IN FRAUD PREVENTION**

The Serious Fraud Investigation Office (SFIO) is a specialized multi-disciplinary agency established by the Central Government under Section 211 of the Companies Act, 2013 for investigating serious and complex cases of corporate fraud. The SFIO consists of experts from diverse fields, including corporate law, accountancy, forensic auditing, taxation, banking, information technology, and capital markets.

Under Section 212 of the Companies Act, 2013, the Central Government may assign an investigation to the SFIO where it is of the opinion that the case involves substantial public interest or requires coordinated investigation. The SFIO has wide powers to summon people, examine records, conduct search and seizure, and arrest individuals where there is reason to believe that they are guilty of offences involving fraud under Section 447 of the Act. Upon completion of its investigation, the SFIO submits a report to the Central Government, and such report is treated as a report filed by a police officer under the Code of Criminal Procedure for the purpose of prosecution.

SFIO has played an important role in major corporate fraud investigations, including the Satyam Computer Services scandal, the Infrastructure Leasing & Financial Services (IL&FS) crisis, and matters connected with large-scale banking and financial frauds. It frequently coordinates with agencies such as the Central Bureau of Investigation (CBI), the Enforcement Directorate (ED), and the Securities and Exchange Board of India (SEBI) to ensure comprehensive investigation and prosecution.

The establishment of the SFIO significantly strengthens the corporate governance framework in India by enhancing regulatory oversight, improving accountability, and ensuring that serious instances of fraud are investigated by a specialized and

independent authority. Its effective functioning serves as an important deterrent against corporate misconduct and contributes to investor confidence and market integrity.

## IX. SUGGESTIONS AND RECOMMENDATIONS

In light of the issues identified in this study, the following suggestions and recommendations are proposed to strengthen corporate governance and improve fraud prevention in Indian companies:

- 1. Strengthening Board Independence:** Companies should ensure that independent directors are selected through a transparent process and are provided with adequate training to effectively supervise management and identify governance risks.
- 2. Enhancing Audit Quality and Auditor Independence:** Mandatory rotation of auditors should be strictly enforced, and audit committees should closely monitor the performance and independence of statutory auditors.
- 3. Improving Internal Controls:** Companies should establish robust internal control systems, periodic internal audits, and risk management mechanisms to detect irregularities at an early stage.
- 4. Technology-Based Fraud Detection:** Listed companies should adopt data analytics, artificial intelligence, and automated monitoring systems to identify suspicious transactions and unusual financial patterns in real time.
- 5. Strengthening Whistle-blower Protection:** Existing vigil mechanisms under the Companies Act, 2013 should be implemented effectively to protect employees and other stakeholders who report misconduct in good faith.
- 6. Timely and Accurate Disclosures:** Companies should comply strictly with disclosure obligations under the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 to ensure transparency and maintain investor confidence.
- 7. Capacity Building of Regulatory Authorities:** Regulatory bodies such as the Serious Fraud Investigation Office (SFIO), SEBI, and the Ministry of Corporate

Affairs should be provided with adequate resources and technological support to conduct prompt and independent investigations.

8. **Promoting Ethical Corporate Culture:** Senior management and boards of directors should foster a culture of integrity, accountability, and compliance through regular training and strong ethical leadership.

## X. CONCLUSION

Corporate governance and fraud prevention are deeply connected. A company that follows strong governance principles is less likely to face fraud. In India, corporate governance has evolved significantly due to reforms and regulations like Companies Act, 2013 and SEBI LODR Regulations. These reforms introduced independent directors, audit committees, disclosure requirements, internal audit, and whistleblower policies.

However, fraud still occurs because governance is sometimes treated as a formality rather than a real ethical responsibility. Many companies still face challenges like promoter dominance, lack of transparency, weak enforcement, and poor internal control.

Fraud prevention is not possible only through laws. Companies must build a culture of honesty, accountability, and transparency. Boards should be active and responsible. Audit committees must work effectively. Auditors must be independent. Technology should be used to monitor transactions and detect fraud early.

In conclusion, India has made strong progress in corporate governance, but strict implementation, awareness, ethical leadership, and technology-based monitoring are necessary for long-term fraud prevention and sustainable corporate growth.

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