INTERNATIONAL JOURNAL OF ADVANCE RESEARCH AND DEVELOPMENT

(Volume2, Issue5)
Available online at www.ijarnd.com

Corporate Governance Mechanisms in India

Nidhi Sharma
Maharishi Dayanand University
nidhi.sharma783@gmail.com

ABSTRACT

This paper is about making good mechanism for company's corporate governance. This article further helps in examining the relationship between the two parts of mechanism i.e. internal and external mechanisms of corporate governance. The need for proper governance is to create a culture of transparency, awareness and clearness in the working and operations of corporation. Having a healthy corporate governance, it ensures a company in achieving long term goals and maximising long term company value as well as goodwill. In this paper we further put focus on how to keep the stakeholders interest safe and assist in reducing agency costs and clear by providing statutory provisions created by different regulatory bodies for the company. Regulatory framework assists the firm in improving their practices as well helps in creating better output and performance.

Keywords: Corporate Governance; Corporate Governance Mechanisms, Statutory Framework, Shareholders Rights and Interest, Information Transparency, and Disclosure, Accountability.

INTRODUCTION

Over the last decades, corporate governance is a topic of group discussion which cannot be avoided in corporate boardrooms. Lots of social events and other factors are held responsible behind this inevitability. In India, the most important aspect of corporate governance is its regulations and their bodies. These regulatory authorities seek organisations to keep a check on management policies and strategies for safeguarding stakeholder's rights. Here a question arises, why do these regulatory bodies need to intervene in company's management policies? Why make it mandatory for the firms to follow the rules designed and incorporated by the regulatory assignees irrespective of not having all the relevant information to focus upon. Although these rules must be designed with the best intention of providing adequate safety and protection to the stakeholders. It can be the other side if regulators adopt giving preference to one group of employees over the other. By keeping in mind all the perspectives, we found three reasons behind the intervention of regulators in corporate governance of the firms.

One of the reason comes in front as if one of the members of regulatory bodies is the founder of the firm then there is certainty of favoritism within the employees of the firm or with external parties. This may lead to provocation of governance mechanism in regard to the society which further needs to be specified with the intervention of legislation. In order to simplify the complicated business processes due to favoritism, regulatory bodies help the firm in enhancing the corporate governance mechanism in a beautiful way.

The other reason of intervention found here that in case the various aspects of governance became legally mandatory by regulators, then companies need to follow those practices like ticking checklists and other such practices rather give more significance to corporate governance systems. This way the need for intervention of outside parties arises. The third reason behind the interference is related to having a feeling of insecurity among the company management regarding excessive interference. Management sometimes feels that due to the excessive involvement of outside parties, the operations and functioning of business may fluctuate. Here regulatory bodies' needs to give an assurance to the management of the firm that their intervention is limited to few aspects of the firm which needs to be corrected in order to improve the governance of the firm and the intervention should not take place inadvertently.

REVIEWS ON GOVERNANCE MECHANISMS IMPACT ON CORPORATE WORLD

According to Desai (2000), corporate governance of a firm must follow certain things. There must be proper guidelines to be issued concerning with minimum capital and amendments of a number of auditors, there must be proper delegation of responsibilities among the board members of a company, there must be proper implications towards SEBI rules and regulations adoption.

The other two authors have given their viewpoints concerning with few parameters of corporate governance. Dwivedi and Jain (2005) have given their focus on board meetings, board size, shareholdings of foreign and institutional investors in their study. Around 350 Indian listed companies from the period of 1997-2001 had been taken by the authors of their research study.

Tuteja (2006) has given their stress more on Board of the structure of the company. Around 100 Indian companies were studied for the research purpose concerning with structure of corporate management. Further, he concluded that chief executive officer was the higher in authorities and responsibilities under the Board of Directors team. Having followed by new rules and policies related to corporate governance, non-executive directors were higher in power in comparison to company boards.

Another author Bhattacharya, CB. et al in McKinsey Report (2011) discussed that proper social corporate responsibility should be adopted by the firms in order to achieve the financial and performance goals. It is clear that investors invest in the firms who offers good and tangible benefits by adopting good governance mechanisms. Good governance not only ensures proper transparency and answerability for the stakeholders but also ensures better productivity and output for the firm. In the corporate world, the major tycoons of business like Tata and BIRLA Groups, Mahindra Group, Infosys, L& T and more other private enterprises are giving more and more emphasis to better governance culture to be adopted within the organisation. Many listed firms have also given their prominence to better corporate governance. These firms include Gas Authorities of India, Oil and Natural Gas Corporation, Bharat Electronics Limited, Bharat Heavy Electricals Limited, and so on.

Bhalla (2012) have more focussed on the perception levels of managers related to corporate governance. For the survey, different sort of public and private firms was analysed from India and as a conclusion, it was found that there is a relationship between the satisfaction levels of investors with the performance of the firm in relation with following corporate governance practices.
A conventionally lot of researches have been done concerning with Corporate governance mechanisms. Narayanaswamy, R. et al, 2012, has given a brief outline in this governance concept. He has mentioned in his research about the contribution of major events to the practices of corporate governance since economic deregulations in 1991. He has provided further implications as well concerning with accounting practices to be adopted for Indian corporate governance. Due to advanced changes in the corporate world, Indian industries are now adopting new modern technologies, harnessing new innovations in their product policies in accordance with new corporate governance policies.

GOVERNANCE MECHANISMS

A certain set of authorities and responsibilities which have an influential power on management decisions and eliminates the managers' discretionary space is termed as corporate governance mechanisms. These mechanisms act as a controlling tool for creating a balance between principals and agents cost and further ensures in safeguarding the interests of stakeholders. According to Hill & Jones, 2004, corporate governance mechanisms are the systems that make a better coordination between the agent and principal relationship. Basically, two types of mechanisms revolve around the corporation environment depending upon the influence and relative importance of these tools. The two mechanisms are constituted by internal and external mechanisms within and outside the firm. The association of internal mechanism includes board of directors, stakeholders, employee's compensation schemes and other internal processes and systems. The need for internal control or mechanism arises when the business goes off track and requires proper monitoring in internal proceedings and further corrective measures are required to be taken. As part of monitoring internal governance, reporting lines are properly defined, operations of business work smoothly which further assist in creating a right path for the organisation by segregating the roles of responsibility, authority, and control in policy development. External governance mechanisms are the tools including auditors, market accessories like market competition, product branding and selling policies, regulatory environment affecting the product, governance code of conduct to be adopted, fluctuations of stock exchanges, creditors and debtors and so on. Generally, external governance mechanism is created by stakeholders of a firm in order to make company operations in accordance with the parties associated with the firm either independent or independent way. External parties at the time of annual general meeting provide suggestions and guidelines to the firm for their best business operations but it is in the hands of organisation whether to follow or ignore them.

Internal Corporate Governance Mechanisms

Internal mechanisms are the ways and methods used by the firms which help the management in enhancing the value of shareholders. The constituents of internal mechanisms include ownership structure, the board of directors, audit committees, compensation board and so on.

- *The Board of Directors:* Board of the Directors is the main peoples of the firm and for the few companies they are the backbones of the business. They have more authorities and responsibilities of the business firm and they keep track on monitoring and controlling all activities of the management in order to maintain the business performance on the track as well as safeguard the interest of stakeholders. Moreover, board of directors is accountable legally for the decisions they make on behalf of their firm and also they are more authorised to hire a new member or employee for the firm. At the time of auditing, they are highly accountable for the financial information provided to them concerning with the firm. There are three types of directors: internal, external and independent directors. Internal directors work within the organisation, external director's work from outside business, they work for several companies on board, independent directors maintain their reputation objectively and present their own way of decisions.
- *Board Committees:* Board committees are the additional part of the board of directors. They are involved in those activities which are assigned by the board of members to them. According to the nature of business, board committees are regulated by the laws and regulations issued by the company. It totally depends on the country's laws and regulations whether the creation of these types of committees should be mandatory for the firm or not.
- *Financial Statements and Auditors:* Financial statements are the information which contains the company data and transactions. Every company needs to present their financial reports on the quarterly and annual basis and get them checked with the auditors. The real picture presented by the auditors reveals the true financial picture of the firm which further becomes the information for the parties involved with the firm either directly or indirectly. On the basis of these financial statements, stakeholders create their statements of action towards the firm. In case they found the reports in positive track, they make up their mind to invest in those firms, on the other side if the stakeholders find the report in the negative side, it will further hamper their trust level in favour of the firms.
- *Ownership Structure:* This is another means of controlling the management part of the company. This way a business can maintain its best monitoring and controlling system for the better performance of all the functioning of the business firm.
- *Stock-Based Compensation:* To eradicate the principle and agent costs issue, the best solution is to provide shareholders interest on time and proper compensation to the employees. Stock-based compensation helps the shareholders in motivating the internal managers for achieving the long terms objectives of the company.

External Corporate Governance Mechanisms

Sometimes internal mechanism lacks in itself while performing the best for the company. This time external factors play a vital role in controlling the corporate governance mechanism of the business firm. The constituents of external governance mechanism include market factors, intermediaries, goods and services prevailing in the market, managers of labour market etc.

- *The Financial Market:* Stock market plays a significant role in firm's ups and downs. There is a direct relation between the market value of the firm and the efficiency of the managers. In case if the shareholders start selling the shares of the company due to somehow reason and if the process is going on in large number further then naturally the market value of the firm starts declining. This way the company who is losing its market value may become the target of acquisition with the help of other big company. Due to the threat of acquisition, the management of the firm can adopt the negative actions like adopting agency costs policy or any other strategy in order to safeguard their business.
- *The Market of Goods and Services:* Competition is another factor which leads the business firm. If the society does not like the products and services offered by a business firm then it becomes natural that their business starts declining and further it may lead to a reduction in the profits ratio of the business firm. Thus company needs to adopt timely researchers and survey in order to tap the resources in accordance with the market requirements.
- *The Labour Market for Managers:* In controlling process, human capital is the concept which can be sometimes controlled and sometimes not. If the managers are highly conservative and strict to their employees than the labour market can go in against with the business and may harm the resources of the firm in order to fulfill their demands. This process needs a proper selection of competent manager (who

controls the lower class employees) should be done in order to create a proper balance of coordination between the managers and the employees.

Issues/Mechanisms
The prevailing issue behind poor corporate governance mechanism found in Indian corporate sector is that most of the firms are family structure. Most of the so-called shareholders are related entities who does not need to enquire about the better governance of the firm. Therefore these types of firms need proper monitoring and controlling mechanism in order create proper governance. Further, the problem exaggerates that as the company has higher number of relatives in terms of stakeholders and owners, it is certain that the most of the business transactions can be related to known parties. After research, it is found out that a big number of Indian listed companies are affiliates or divisions of MNC's (Multinational companies). As per the FEMA Act and their regulations, the company must follow all statutory requirement while making transfers from Parent Company to Division Company. Here companies try to avoid following that statutory requirement due to having stuck in long procedures and formalities. All such activities are due to having business transactions with familiar parties and in order to get potential gains by doing fair dealings with mostly familiar parties or with businesses of related family members. Such issues undermine the financial market confidence and moreover, it may harm the process of investment mobility in between countries. In order to eliminate such malpractices government of India has set the certain statutory framework which enables in creating a better corporate governance mechanism in the corporate world.

Statutory framework of corporate governance
In general corporate governance is that mechanism with the help of which the management of the organisation can be properly managed, controlled and governed in a specific way. The main objective of governance mechanism is to make ensure that the rights of stakeholders could not be curbed by the internal management of the company and moreover company management should be held accountable towards their stakeholder in order to keep trust and safeguard their interest. In order to confirm a proper corporate governance mechanism, the government of India has built a certain set of standards or in other words a statutory framework for the corporate world.
By taking into consideration of international best mechanisms, the Indian government has set these statutory framework concerning with corporate governance. Following list ensures the major agreements come under that statutory framework:

1. Stock exchanges carrying standard listing agreement: these agreement are to be signed by the companies who have their stocks listed on stock exchanges.
2. The Companies Act, 2013: this act ensures proper accountability and transparency of the firm as all companies must ensure that they follow all the statutory provisions related to board meetings and conferences, audit committees, business transactions related to other parties, disclosures of all financial statements and so on.
3. Accounting norms and standards: Accounting norms and standards are the provisions set by Institute of Chartered Accountants of India (ICAI). According to New Companies Act, Section 129, there must be transparency in all companies' accounts and policies. Moreover, ICAI ensures that the items involved in financial statements of the company must be as per the accounting norms and standards.
4. SEBI (Securities and Exchange Board of India) guidelines: SEBI is the authority of regulation who controls the listed firms and issues various guidelines, rules and regulations in terms of keeping investors interest safe.
5. Secretarial Standards issued by the Institute of Company Secretaries of India (ICSI): This regulatory body is an autonomous body which issues a certain set of standards and provisions come under New Companies Act. There are two standards issued by Institute of Company Secretaries of India i.e. SS-1, Meetings of the Board of Directors and another is SS-2, Secretarial Standards on General Meetings. These types of provisions came into force on July 1, 2015.

Further, the companies Act 2013, has increased the levels of discussion topics in the Board Meeting of India. New topics may include gender diversity not to be involved, the disclosure of norms and standards, women directors' enhancement in management, delegating corporate social responsibility, increasing the role of Independent Directors, keeping safeguard for the interest of minority shareholders, and creating certain benchmarks for better corporate governance. In a global perspective, a good corporate governance mechanism must be created in order to improve the environment of the business in terms of faith, clarity, and answerability. Good mechanism helps in supporting sustainable growth and financial stability for the organisation.

CONCLUSIONS
This paper reflects the significance of corporate governance practices in firm's overall performance. We have given focus on few historical types of research related to corporate governance in India. Further, the article

emphasised on the causes and issues affecting the corporate business due to lack of proper corporate governance or sometimes due to inadvertently neglecting the governance practices for creating misleading interpretations. Various types of mechanisms were then discussed related to governance i.e. internal and external mechanisms. In the article, the significance of proper corporate governance mechanism has been talking over. Proper regulations created by Indian government were highlighted with the help of which sick companies could still have scope to create their future bright in near future. But here companies need to face lots of challenges come in their way and follow all the norms and standards set by the governance in order to create an impact of better governance practices on companies future performance.

Generally speaking, corporate governance is an inevitable topic for companies nowadays. Investors are more aware of the governance significance on the firms' performance. A good corporate governance builds up stakeholders' confidence and helps them in keeping their interests safe. This concept is also an important concept for foreign investors as well. It keeps investors well versed about the various plans and policies, rules and regulations about the company. Overall we concluded here that corporate governance is the key to introducing accountability, flexibility, and transparency in decision making, and other measures of the company which not only fosters in safeguarding the stakeholder's interest but also reflects a positive picture of the financial performance of the company. Ultimately it helps in enhancing the economic progress of the country as well.

REFERENCES

1. Afsharipour, A. (2009), "Corporate Governance Convergence: Lessons from the Indian Experience", UC Davis Legal Studies Research Paper Series, p. 181.
2. Aggarwal, R. (2010), "Independent Directors: time to introspect, suspect, respect: An Indian perspective", Journal of Indian Business Research, Vol. 2.2
3. Asian Corporate Governance Association, 2010, ACGA White Paper on Corporate Governance in India, Hong Kong, Jan. 2010.
4. Balasubramanian, N. et al. (2009), Firm level corporate governance in emerging markets: A case study of India, Social Science Research Network, pp 319-340.S. Batra (2008), Background document prepared for the 2008 Asian roundtable on corporate governance, Hong Kong May 2008.
5. Bhardwaj, H. (2011), "Corporate governance in India: Towards a more holistic approach", Oxford Student Legal Research Paper Series, 04/2011.
6. Bose, S. (2005), "Securities markets regulation: Lessons from US and Indian Experience", Money and Finance, Jan-June, pp 83-124.
7. Chakrabarti, R. W. Megginson and P. Yadav (2008), "Corporate Governance in India", Journal of Applied Corporate Finance, Vol. 20, no. 1.
8. Chakrabarti, R., K. Subramanian and F. Tung (2010), Independent directors and firm value: Evidence from an emerging market, SSRN 1631710.
9. Global Corporate Governance Forum (2011), "Culture and corporate Governance Principles in India: Reconcilable Clashes", Private Sector Opinion, p. 23.
10. Institute of Company Secretaries of India (2010), Guidance Note on Related party transactions, New Delhi.
11. Jackling, B. and S. Johl (2009), "Board Structure and Firm Performance: Evidence from India's Top Companies", Corporate Governance: an International Review, 17 (4).
12. Kali, R. and J. Sarkar (2011), "Diversification and Tunnelling: Evidence from Indian business Groups", Journal of Comparative Economics.
13. Siva Prasad Ravi, "Corporate Governance in India: Challenges for Emerging Economic Super Power", Business Studies Journal, Supplement 2, Vol. 6, pp. 1-17, 2014.
14. Jaya Bhalla, "Corporate Governance: Perception of Executives in India", Review of Management, Vol. 2, No. 1/2, pp. 35-43, 2012.
15. S. K. Tuteja, "Board Structure in Indian Companies – An empirical survey", Journal of Management Research, Vol. 6, No. 3, pp. 149-155, 2006.
16. Neeraj Dwivedi and Arun Kumar Jain, "Corporate Governance and performance of Indian Firms: The Effect of Board Size and Ownership", Employee Responsibilities and Rights Journal, Vol. 17, No. 3, pp. 161-171, 2005.
17. Suresh Thakur Desai, "A beginning of Corporate Governance" Chemical Business, Vol. 14, No. 2, pp. 42-44, 2000.
18. Y. R. K. Reddy, "The ethics of corporate governance: An Asian perspective", International Journal of Law and Management, Vol. 51, No. 1, pp. 17-26, 2009.
19. T. N. Satheesh Kumar, 'Corporate Governance: Principles and Practices', Pearson Education India; 4 edition (2011).

20. P. De Andres and E. Vallelado, Corporate Governance in Banking: The Role of the Board of Directors, Journal of Banking & Finance, 32, (2008), 2570 – 2580.
21. F. Mishkin and S. Eakins, Financial Markets and Institutions, Pearson-Prentice Hall, Boston, 2009.
22. Basel Committee on Banking Supervision, Enhancing Corporate Governance for Banking Organization: Banking for International Settlement, 2005.
23. IMF World Outlook Database, April 2014, FGB, Investor Presentation, April/May 2014
24. Prasad K, 'Corporate Governance', Prentice Hall India Learning Private Limited; 2 edition (2011).
25. Asish K. Bhattacharyya, 'Corporate Governance in India: Change and Continuity', Oxford University Press (19 September 2016).

WEB REFERENCES

https://elearn.uta.edu/bbcswebdav/users/jmcgee/Syllabus/Content/Syllabus%20and%20Course%20Content/pdf/Chapter%2011.pdf

http://www.personal.kent.edu/~vberardi/44285/44285--ch10notes.pdf

https://link.springer.com/chapter/10.1007%2F978-1-4615-1095-6_10#page-1

http://smallbusiness.chron.com/three-types-corporate-governance-mechanisms-66711.html

https://www.oecd.org/daf/ca/Improving-Corporate-Governance-India.pdf

http://www.mondaq.com/india/x/456460/Shareholders/Corporate+Governance+Framework+In+India

https://www2.deloitte.com/content/dam/Deloitte/in/Documents/risk/Corporate%20Governance/in-risk-global-trends-in-corporate-governance-4Dec2015-noexp.pdf

