A STUDY ON SIGNIFICANCE AND IMPACT OF CORPORATE GOVERNANCE

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Abstract: The concept of Corporate Governance dates back to the emergence of capitalism and modern stock organizations, development of global trade, and enormous growth of multinational firms during industrial revolution (Erismann-peyer, Steger & Salzmann, 2008). Internal and external stakeholders of corporations are striving to strengthen their assessment of the soundness of corporate governance practices within corporate bodies (Mark, 2011). It is the buzzword in today's business environment is a combination of legal practices, ethics, best management practices, wealth creation management. It is relevant to developing, transition and emerging-market economies, in view of the assertion that these countries lack vibrant, long-established financial institutions to deal with issues related to corporate governance (McGee,2009). It mainly targets the long term life of the economic entity and aims to protect the interests of the shareholders in the management of the organization. The two objectives of the corporate governance are: mitigating the risk of the economic enterprises by improving and enhancing the transparency and responsiveness; and long term efficiency of the organization through avoiding dictator behaviours and non-responsibility of the executives (hassas Yeganeh, 2009). Institutional shareholding and its impact on making financial and managerial decisions are the issues that the firms might be confronted with (Rahanama Roudposhti and Aslani, 2008).
To achieve objectives of optimum allocation of resources, the officials and the policy makers should create the legal setting and monitoring agents and provide a secured environment for the economic and investment operations (Hosseini and Rahbari, 2008). Corporate Governance is a set of the relationship between Executives, Board of Directors, shareholders, stakeholders who intend to create an appropriate structure for adjusting the objectives and determining the ways that these objectives are satisfied and operations are controlled (Kashani Pour and Resayian, 2009). It is also provides a structure by which the objectives are determined and the ways to achieve the goal are clearly identified. (Alnajjar, 2010)

Keywords: Changing Ownership Structure, Importance of Social Responsibility, Growing number of Scams, Indifference on the part of Shareholders, Globalization, Takeovers and Mergers, SEBI

Introduction: Corporate Governance is needed to create a corporate culture of consciousness, transparency and openness. It enables a company to maximize the long term value of the company which is seen in terms of performance of the company. It is believed that the steering agent for the survival and the growth of the company is primarily its "Corporate Governance" policies. Corporate Governance refers to the code of conduct through which companies are directed and controlled whether the company may follow stakeholder or shareholder model. The practices of Corporate Governance is increasingly becoming vital and very crucial point of difference between stakeholder and shareholder value. The increase in financial and managerial scams has led the investors to increasingly look for transparency and professional management in handling the company's business. The concept of corporate governance has been in existence for a long time but it was formalized in UK in the early 1990's.

Concept of Corporate Governance: The concept of corporate governance dates back to the mergence of capitalism and modern stock organizations, development of global trade, and enormous growth of multinational firms during industrial. Internal and external stakeholders of corporations are striving to strengthen their assessment of the soundness of corporate governance practices within corporate bodies. Corporate Governance, the buzzword in today's business environment is a combination of legal practices, ethics, best management practices, wealth creation management and foresight. The Corporate Governance principles play essential roles in maintaining, increasing and optimizing the invested funds, especially for the firms with the initial public offering. It is a set of controlling regulations, policies and guidelines which are aimed to help in achieving the organizational objectives.

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In this paper we look at various concepts like need, importance, impact, challenges of corporate governance, what is qualitative corporate governance and key areas of corporate governance practices followed by company in India. This includes parameters like Board Constitution, Board Structure, Difference committees, Independent directors and their roles, conflicts of Interest and disclosure of information. This objective is to determine if there is a relationship between corporate governance and firm performance. The study tries to see whether higher and better corporate governance leads to better performance of the companies.

Good Corporate Governance and Need of Corporate Governance:

Good Corporate Governance required for build and strengthen accountability, credibility, transparency, integrity, trust, ethical standards and reputation of the organization. The need for corporate governance has arisen because of the increasing concern about the non-compliance of standards of financial reporting and accountability by Board of Directors and management of corporate inflicting heavy losses on investors.

The collapse of international giants likes Enron, World Com of the US and Xerox of Japan are said to be due to the absence of good corporate governance and corrupt practices adopted by Management of these companies and their financial consulting firms.

To achieve objectives of optimum allocation of resources, the officials and the policy makers should create the legal setting and monitoring agents and provide a secured environment for the economic and investment operations (Hosseini and Rahbari, 2008). Corporate Governance also provides a structure by which the objectives are determined and the ways to achieve the goal are clearly identified. (Alnajjar, 2010).

In case of India, in 1999 SEBI realized the need for good corporate governance and for this purpose they constituted a committee under Kumar man glam Birla committee and Narayan Murthy committees to recommend Corporate Governance measures to be followed by India Companies. SEBI felt a need to regularize the disclosures by the companies in the wake of scams like MS shoes etc. After the recommendations of these two committees took the form of Clause 49 of the listing agreement and it was finally implemented in 2006.

Good Governance helps to develop a brand name for the company and it improves the confidence of investors and stakeholders of the company.

Significance / Importance of Corporate Governance: The need, significance or importance of corporate governance is listed below:
a) Changing Ownership Structure: In recent years, the ownership structure of companies has changed a lot. In large organizations public financial institutions, mutual funds, etc. are the single largest shareholders as they are controlling management of the companies. They force the management to use corporate governance. They are putting pressure on management to become more efficient, transparent, accountable, etc. and also ask the management to make consumer-friendly policies, to protect all social groups and to protect the environment. Therefore, the changing ownership structure has resulted in corporate governance.

b) Importance of Social Responsibility: Corporate Governance is very much important in Social responsibility. The Board of Directors have to protect the rights of the customers, employees, shareholders, suppliers, local communities, etc. as it is possible only if they use corporate governance.

c) Growing Number of Scams: Misuse and misappropriation of public money are happening every day in India and worldwide viz. in stock market, banks, financial institutions, companies and government offices. In order to avoid these scams and financial irregularities, many companies have started corporate governance.

d) Indifference on the part of Shareholders: In general, shareholders are inactive in the management of their companies. They only attend the Annual general meeting. Postal ballot is still absent in India. Proxies are not allowed to speak in the meetings. Shareholders associations are not strong. Therefore, directors misuse their power for their own benefits. So, there is a need for corporate governance to protect all the stakeholders of the company.

e) Globalization: Due to introduction of globalization in multinational organizations foreign investors and companies, they have to follow foreign rules and guidelines for which Corporate Governance is to be observed by them, so that it is mandatory to survive and succeed in global market.

f) Takeovers and Mergers: Sometimes most of the companies are taken over and merging in the corporate business world so that corporate governance is required to protect the interest of all the parties during takeovers and mergers.

g) SEBI: It is mandatory compliance to observe the rules and guidelines applied by for certain companies. This is done to protect the interest of the investors and other stakeholders.

h) Changing Ownership Structure: Now a day there is introduction of conversion of organization in corporate business in which public financial institutions, mutual funds, etc. are single largest shareholder in most of the large companies. So, they have effective control on the management of the companies. They force the management to use corporate governance. That is, they put pressure on the management to become more efficient, transparent, accountable, etc. The also ask the management to make consumer-friendly policies, to protect all social groups and to protect the environment. So, the changing ownership structure has resulted in corporate governance.

i) Takeovers and Mergers: In the recent days, so many takeover and mergers in corporate world as it is mandatory to protect the interest of all the parties during takeovers and mergers.

Impact of Corporate Governance: Research on the importance of generally accepted “best practices” in corporate governance has generally failed to find convincing connections between these practices and organizational performance. We propose four possibilities for this tenuous relationship, that are not mutually exclusive : firstly, the possibility that “Best Practices” in governance are indeed irrelevant to organizational performance, secondly, that the operationalization of theoretical concepts has low face validity; thirdly, that studies are too narrow, aiming to relate board attributes directly to organizational performance and ignoring other systemic factors; and lastly, the possibility that different types of organizations require different practices in corporate governance.

Good governance has always been an important element in human interactions and in an increasingly uncertain global climate has now become an imperative. Business and economy are closely aligned to the fortunes and well-being of people which makes corporate governance a subject of great importance. Therefore, to maximize impact, aspiring and current board members must possess an in-depth understanding of how corporate boards work and what it takes to lead with transparency; accountability and efficiency. By examining today’s corporate governance challenges, these programs position prospective female board members, well as seasoned chairs, committees, and individual directors to positively influence your company’s direction and shareholder performance.

Major Challenges of Corporate Governance: Corporate Governance Reforms in India now stand at an interesting crossroads, and the future development of the next generation reforms, and in their implementation during the current decade, will decide how effective, they are for Indian business The Companies Act 2013 envisages radical changes in the area of Corporate Governance and is set to have far-reaching implications. The new regime is expected to significantly change the manner in which corporates operate in India. While the bar for corporate governance has been raised, the penal consequences have been exponentially increased with a large number of sections reserving provisions for the prosecution of directors, officers in default and key managerial personnel. There is a clear shift towards closely monitoring unlisted public companies and large private companies with enhanced compliance requirements encompassing disclosures, transparency and governance procedures.

Following are some major challenges in corporate governance:
a) To achieve excellence in Corporate Governance -
b) To permanently meet the mix of — strict legal regulations — regulatory requirements —
c) softer best practice guidelines
d) Global applicability versus compliance with local jurisdiction
e) Conflicting rules in a transborder environment
f) Timely implementation of best Corporate Governance throughout the Group
g) Consistency in internal rules and regulations
h) Internal controls and documentation
i) Education and Training
j) Conflict between the dominant and minority shareholders
k) The dilemma of micro-management
l) Companies to implement corporate governance reform measures
m) Real independent directors
n) Regulatory oversight including multiplicity of regulators
o) Linkage of good governance to good performance
p) Risk assessment, Management & Mitigation
q) Integrity and ethical behavior

Qualitative Corporate Governance: Having identified that the required corporate governance standards are rising and that there is increasing scrutiny of quantitative governance by shareholders and regulators alike, what can companies do to reduce the risks they face? Naturally they should ensure that they adopt sound quantitative governance practices as these are now an accepted essential for any company. However, these will be inadequate if that is all a company achieves. The boards (both supervisory and management) need to embrace qualitative corporate governance in order to reduce the risk of scandal, legal action and the resulting damage to reputation. Clearly this involves embracing the true spirit underlying good corporate governance not merely the trappings.

One tool for introducing this features in both the UK Combined Code and the new draft Netherlands Code, namely board evaluations. In the UK the Combined Code encourages companies to undertake a board evaluation annually, preferably with the assistance of an outside organization to ensure that it is robust and the role of the independent board members (in Slovakia the supervisory boards) in such an exercise is paramount if it is to be an effective tool for qualitative corporate governance as opposed to merely a quantitative exercise. As such it is an excellent tool for board members keen to fulfill their role as guardians of good governance of the company.

Key Areas of Impact: While there are changes across the board, the key impact areas in the area of corporate governance include the following:

1. Board Structure and Responsibility:
- Enhanced responsibility for the board and its committees
- Specified unlisted companies to have independent directors; mandatory code for
- Independent
- Directors - Mandatory woman director for certain companies
- Mandatory key managerial personnel (Key Managerial Personnel) – Chief Executive
- Officer/
- Managing Director/Whole Time Director, Chief Financial Officer and Company
- Secretary Performance evaluation of board and individual members

2. Disclosures and Reporting:
- Enhanced disclosures and assertions in Directors' Report – risk management, internal
- control for financial reporting, legal compliance, RPT, CSR, etc.
- Compulsory consolidation of accounts; summary statements of associates / Joint
- Ventures subsidiaries
- Disclosures of shareholding pattern
- Disclosures for public money lying unutilized

3. Risk, Controls And Compliances: Boards now obligated to report on the following:
- Development and implementation of risk management policy
- Systems to ensure compliance to all applicable laws and their operating effectiveness
- Internal financial controls and their operating effectiveness (for listed companies)

4. Secretarial Compliances:
- Stricter yet forward-looking procedural requirements for board proceedings:
- Minimum 7 days' notice, board meetings permitted through electronic mode
- Presence of at least one Independent Director must for board meeting at shorter notice
- Gap between two meetings < 120 days
- Compliance of ICSI Secretarial Standards have been mandatory

5. **Related Party Transactions (Related Party Transaction), Loans and Investments**:
- Scope of RPT significantly enhanced; concept of arm's length pricing introduced
- Central government approval not required, however, heavy penalties for noncompliance
- Related Party Transaction disclosure in Directors' Report along with justifications
- Stricter requirements for loans and investments including private companies

6. **Audit and Auditors**:
- Enhanced restrictions on appointment and rotation of auditors
- Statutory auditors prohibited from providing certain services
- Enhanced powers and role of auditors
- Mandatory internal audit and secretarial audit for prescribed class of companies
- Auditors to report on internal financial controls and their operating effectiveness

7. Corporate Social Responsibility Prescribed Class of Companies To:
- Form a CSR committee with at least one Independent Director
- Form and approve a Corporate Social Responsibility policy
- Endeavour to spend at least 2% of net profits o Directors to explain inability to spend
- in the directors' report

Conclusion: Good Corporate Governance does not only mean to apply rules and to meet requirements but it is definitely more than that. Although there is no widely accepted definition or model of Corporate Governance. Good Corporate Governance can only be achieved with top representatives as role models, demonstrating credibility and integrity on a daily basis. These are the determining elements that constitute sustainability in Corporate Governance.

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