Research Paper Commerce

Corporate Governance in Business Enterprise

*Archana J. Bhoot

* Assistant Professor, Government commerce college, Kubernagar, Ahmedabad

ABSTRACT

Good corporate governance leads to development of a framework that provides adequate protection to the interests of stakeholders and reinforces the fiduciary responsibilities of those vested with the authority to act on behalf of the stakeholders. Corporate governance encourages companies and those who own and manage them to achieve their corporate objectives through a more efficient use of resources. Moreover, corporate governance framework should recognize the rights of stakeholders as established by law.

Keywords : Corporate Governance: Important, Affect Market Valuation, Development ,Role of management and / Board of Directors, Relationship between share price and corporate governance, Corporate

Introduction :

Over the last two decades, corporate governance has attracted a great deal of public interest because of its apparent importance for the economic health of corporations and society in general. The headlines of the previous two years in particular portrayed a sad story of corporate ethics. Corporate governance involves established internal control systems for identifying, managing and monitoring risk. Corporate governance is a system by which companies are directed and controlled. Corporate governance can also mean a set of arrangements in place to make a company accountable to its stakeholders. In the current dispensation, good corporate governance is not only a statutory requirement but a necessity to attract investors. It needs to be in place to assure investors that potential risks facing the company are under control. Departments like internal audit control are located in the company to check compliance with internal standards and standards set by regulatory bodies.

Definitions of Corporate governance:

“Corporate governance is the system by which business corporations are directed and controlled. The corporate governance structure specifies the distribution of rights and responsibilities among different participants in the corporation, such as, the board, managers, shareholders and other stakeholders and spells out the rules and procedures for making decisions in corporate affairs. By doing this, it also provides the structure through which the company objectives are set and the means of attaining those objectives and monitoring performance”-By Organization for Economic Cooperation and Development

Corporate governance is the set of processes, customs, policies, laws, and institutions affecting the way a corporation (or company) is directed The process by which agencies are directed and controlled. It is generally understood to encompass authority, accountability, stewardship, leadership, direction and control.

Important of Corporate Governance:

When a JSC (join stock company)borrows money, the relationship between the debtor (JSC) and creditor (bank or bondholder) is outlined in a legal agreement between the parties. When a JSC raises capital by selling shares, it enters into a more flexible relationship with its shareholders. The terms of the relationship are as follows: By buying shares in a JSC, an investor supplies necessary capital to the JSC and becomes an owner, or shareholder,in the JSC. In return for this capital, the JSC grants rights to the shareholder: information rights, voting rights and financial rights. a Market Economy.) Corporate governance provides a framework for defining the rights and responsibilities of the various parties within a JSC and understanding their interaction. A sound understanding of corporate governance enables each party to plan and implement a strategy for achieving its goals and representing its interests. It also permits each party to evaluate the behavior of other parties.

How does Corporate Governance Affect Market Valuation?

In both developed capital markets and economies in transition a relationship exists between good governance and market valuation .In developed capital markets, investors make two general assumptions before investing in shares. They assume: first, that the JSC’s governance structure will comply with legal requirements; and second, that the JSC will provide detailed information about its activities, financial status, governance and share capital structure. Investors analyze this information in order to make informed investment decisions. Furthermore, shareholders react to JSC compliance and disclosure in two ways: first, by deciding to buy and sell shares; and second, by voting at general meetings of shareholders.

Development of corporate governance :

In the 1800s, state corporation laws assisted in the creation of corporate boards, who could govern, much like state congresses, without unanimous consent of shareholders. This made the running of corporations much more efficient. As time passes, corporate boards seem to be gathering more and more power, particularly with the inception of large mutual funds and similar cash-building entities, which place another layer of organization between stakeholders and corporate governors.

Fortunately, most people directly involved in corporate governance are honest and interested in what’s best for the company, though there have been glaring and destructive exceptions to that lately. Parties involved directly in corporate governance do not just include the Board of Directors, but also the SEC, the company’s CEO, management, and the more important shareholders. Shareholders typically delegate their decision-making rights to managers to act in their best interests.

Corporate governance is based largely on trust – the trust, by the stakeholders, that revenues will be fairly shared, and that those directly involved in running the company are running it in an aboveboard, honest, and open manner, and that they represent the best interests of the company and of the shareholders. Therefore, key elements of corporate governance are honesty, trust and integrity, openness, responsibility, and accountability. Recent new governmental regulation has attempted to reinforce these elements.

Role of management and / Board of Directors:
Board of directors are appointed to act on behalf of the shareholders to run the day to day affairs of the business. The board also appoints management to run the company. A board's main purpose is to ensure the company's continuous prosperity by directing the company's affairs, whilst meeting the appropriate interests of shareholders and relevant stakeholders.

- The boards must simultaneously be entrepreneurial and drive the business forward but devoid of negligence and excessive risk taking.
- The board should be adequately knowledgeable about the core business of the company and to be answerable for its actions. the dose not mean that they should over influence management of the company.
- The board must be sensitive to the pressures of short-term issues and yet be informed about broader, long-term trends.
- The board must be knowledgeable about local issues and the competitive landscape they are operating.
- The board is expected to be focused upon the commercial needs of its business while acting responsibly towards its employees, business partners and society as a whole.

Relationship between share price and corporate governance: Stock prices reflect the value of a stock at a given point in time. Investor perception about a company can adversely or favorably affect stock price. If stock prices are high, it gives investors value. Management would equally benefit if they have incentives or bonuses tied to the performance of the company's share price. The company would as well benefits if they are seeking extra funding through right issue for example. If companies do not manage their relationship with investors, they have to do damage control after that has affected their stock price adversely on the stock market. Cost management determines profit and dividend- if the company is able to manage its cost effectively and make informed investments, at the end of the financial year, its profits would increase, some portion ploughed back into the business and the rest paid out as dividend to shareholders. Cost can be effectively managed if the right corporate governance is in place to reduce fraud and wastage through negligence.

Corporate Governance for Small & medium enterprise :
There is no universally accepted definition of corporate governance. It is a basically a set of relationships between a company's board, management, its shareholders and the society within an institutional framework. These relationships evolve into the corporate governance framework, which is "the system by which companies are directed and controlled". It is essential to recognize that every company operates within a 'unique' jurisdiction of its stakeholders including investors, creditors, employees, managers, and regulators. Good corporate governance seeks to create an institutional framework that encourages all participants to contribute towards better corporate performance aligned with good governance practices. As has been aptly described by Sir Adrian Cadbury in the preface to the World Bank publication 'Corporate Governance: A Framework for Implementation' (September 1999): "Corporate governance is concerned with holding the balance between economic and social goals and between individual and communal goals. The governance framework is there to encourage the efficient use of resources and equally to require accountability for the stewardship of those resources. The aim is to align as nearly as possible the interests of individuals, corporations and society."

Corporate governance is a significant factor in improving economic efficiency and growth. It has been empirically tested that good governance practices of a company gives a positive signal to investors. With the globalization of markets, international capital flows have become extremely valuable source of external financing. It is essential for companies to observe good corporate governance standards in order to competitively operate in the global capital market and to attract long-term foreign capital. Foreign Direct Investment, which leads to the transfer of technology, is an important factor for economic progress of developing countries. Both the foreign and local investors give importance to good governance practices. In this regard both individual and institutional investors play a role although role of institutional investors is more significant. Therefore good corporate governance is likely to reduce the cost of capital, encourage more stable sources of financing and facilitate the broadening and deepening of local capital markets.

Business Ethics:
Business ethics is defined as a process for integrating values such as honesty, trust, transparency and fairness into its policies, practices and decision making. Business ethics is therefore inherently linked with corporate governance. The importance of business ethics cannot be denied. The old English proverb "as you sow so shall you reap" is indicative of the significance of business ethics. A firm which applies ethical practices also expects to be dealt ethically. These expectations and consequent adoption of ethical practices create chain effect in terms of promoting ethical practices. While the larger firms have already developed their reputation by adopting these ethics, SMEs around the world are increasingly becoming aware of the importance of good, trusting relationships with customers, employees, suppliers and the community.

Conclusion :
The government should facilitate access to financing and equity markets for firms which implement corporate governance. In order to promote entrepreneurial culture, venture capital firms should also be encouraged through enabling regulatory environment. The developing countries need to reform judicial and legal system in order to ensure investor protection The Code should be developed with the consultation and ownership of SMEs and it should be flexible to incorporate different features of corporate governance for firms at different stages in the business cycle, according to the capabilities of the company and the needs of investors. In other words, the Code of Corporate Governance should be a living document. Corporate Governance Unit within the regulator should be strengthened so that it can provide guidance to SMEs on issues related to corporate governance.