1.1 Introduction: Firms and Corporations:

In the 21st Century, especially after making the world economies free for trades and exchanges of resources without any boundary barriers between the geographical demarcations of them; modern corporations have contributed so much to the growth of these all market-driven capitalist world economies. Among these corporations, the joint stock companies have been proved themselves as the nucleus of all business activities in these modern economies. These kinds of corporations are incorporated under the Companies’ Acts of different economies in the form of either industrial unit or commercial venture or any other business enterprises with different size and degree of operations. Most of the world economies’ major capital force is controlled and managed by few such kinds of corporations. Many lawyers and economists describe the corporation as “a nexus of contracts” leading towards its creation and existence. According to Chief Justice John Marshall, “A corporation is an artificial being, invisible, intangible, and existing only in the contemplation of the law. Being the mare creature of the law, it possesses only those properties which the charter of its creation confers on it, either expressly or as incidental to its very existence. These acts are supposedly best calculated to effect the object for which it was created. Among the most important properties are immortality, and, if the expression be allowed, individuality; which a perpetual succession of many persons are considered the same, and may act as a single individual.”

Since the ancient days, the business activities have been carried out in different forms and varied structure of its incorporation. A Business Firm is incorporated, structured and conceded to carry-out its operation primarily for making profit for its investors. Since those days, assorted kinds of business activities under varied forms of business firms have been undertaken and grown till today modern forms of business outlets. When it is a sole proprietorship, it is meant for the only stockholder of this firm, who is known as sole proprietor of his firm. The whole functioning of this firm is undertaken by its sole proprietor himself and hence the profit is also entitled to him only. In this case the governance of the firm is aligned to its objectives spotlessly. If it is a partnership firm, it is meant for many investors of the firm, who all are known as partners of the firm. Herein, the governance of the firm is by and large aligned with its objectives since the management of this firm is controlled by most of the investors of
it. While in the case of the firm as a company, the meaning of making profit gets
diverted and diluted slightly. In the case of such firms, an association of persons,
moreover swell widely, contributes their money to a common corpus known as
company. However, a firm in the form of a company is managed by different set of
people known as the managers. This establishes the separation of ownership and
management of this kind of firms. Therefore, the alliance of the firms’ objectives and
its appropriate governance has become a subject of the burning discussion throughout
the world. This has prompted the twenty first century marked as the emergence of
corporate governance. Corporations in the very stronghold of capitalism, the United
States of America, were hindered in evils and were going through a grave crisis of
credibility during the very early years of the new millennium.

The companies that were apprehended till then as role models in corporate
governance were being endangered with widespread exposure of accounting
irregularities and fraudulent practices. The Security and Exchange Commission (SEC)
set up under the New Deal to combat the Great Depression, emerged to be
inefficiently set to deal with enormous business conglomerates such as Xerox,
WorldCom and Enron that committed conscious swindles with a view to heightening
their sales revenues and for showing highly exaggerated profits. If company
managements want the market value of their equity shares to climb new hikes year
after year, the appeal to fabricate accounts and thereby take credit for unjustified
profits look like to be complicated to resist. Investors, on their part, can neither
compare high profits shown by their companies as a sure index of corporate efficiency
nor treat a company’s collapse to maintain a consistent high profit a failure of
corporate governance.

In twenty first century, governance has become the hottest subject in every field,
especially where the people elected, selected or appointed government is empowered
to rule out and manage the operations and functions of the firm. Corporate
Governance gains greater importance since it is the largest sector in any country
involving most of the human and natural resources and making the largest
contribution to the economic development of a country. This is the fundamental needs
of an economy to grow. Though the magnitude of corporate governance was always
embedded, its relevance discovered to the force only after the crisis created by
Maxwell Communication, Enron, Worldcom, Prmalat, PolyPeck International, Lehman Brothers, Satyam Computers and many more in diverse economies. General Human Tendency is accustomed to lock the stable after the horses are stolen. At the beginning of twenty first century, with god grace, people stirred to the situation before all the horses were stolen. That is why, beyond the bare minimum legal obligations to be complied with, most of the economies have merged with establishing many institutions to deal with all mechanism set in promoting good corporate governance. This practice extends its wings towards establishing the roles, responsibilities, rights and duties of shareholders, board of directors, auditors and other stakeholders to safeguard the interests of all of them. This has been achieved with setting the code of corporate governance containing the detail guidelines for the companies to strengthen their governance. Since the early 1990s regulatory authorities, government sponsored committees, business associations and investors associations in many countries of the world have developed governance practices laying down either the minimum standards or the best practices of corporate governance.

The comparative corporate governance literature has described corporate governance practices along with several dimensions in different economies. The important being the ownership structures, identity of shareholders and financial structure of companies, capital markets, role of financial institutions, workers participation, legal protection and corporate philosophy are the other notable dimensions which have attracted the attention wide span of the academicians and researchers’ fraternity.

1.2 Outline of Indian Firms:
Indian economy, since the ancient days, has been immersed from very cultured and traditional natural resources and related trades and industries undertaken by diverse forms of the Indian Firms. This has made it transformed from the conventional livelihood products’ making and offering till the modern industrial and institutional products and services of the internationals standards to be made available for the rest of the whole world. In India too, the business activities have been carried out in different forms and varied structure of its incorporation starting from a sole proprietorship firm to a partnership firm and leading till the firms known as company. The meaning of making profit gets diverted and diluted slightly for the each kind of
firms in Indian economy also. Before the inception of East India Company in 1600 AD, most of the Indian business firms were in the pattern of either sole proprietorship of partnership in a very less numbers. In this line, the modern form of company has its origin in the legislative enlargements in the mid-nineteenth century in the United Kingdom. Industrial revolution in India along with the development of corporate culture started mostly after the independence in 1947. Conversely, with the distinctiveness of the country’s governance enduring to be feudalistic and its political system deteriorating to be pseudo-democratic, the governance of most of the country’s industrial and business firms flourished on unethical practices at the market place while showing scarce regard for the timeless human and organizational values in dealing with their employees, shareholders and customers.

Truly speaking, the Indian Companies have been conventionally viewed as shareholder-focused entity. Whose main objectives have been of maximizing the corporate profit and return on its investments made by these shareholders. The managers and directors of these firms are principally meant to discharge their duties in these interests only. Until 1993, the Indian Corporate culture thus, denied the participation of employees and others in the routine corporate affairs of these firms. But the initiation of Liberalization, Privatization and Globalization then by Indian Government has opened the doors of its corporate culture with the tremendous growth in Indian Companies. This reinforced the idea of a company being beyond profit maximization and leading towards being a form of organization the business to reap the benefits of large scale of business for many stakeholders. Thus, an alternative conception of a company emerged where the shareholders have begun to be regarded as investors and not the proprietors of the firm. The companies have become the significant part of the society. Along with the obligation of fair returns on the shareholders’ investment, the companies owe certain obligations to their other constituents too.

Despite having a long corporate history evolving from the enactment of the first Companies Act in 1850, the Indian corporate world embedded the substance of corporate governance only after 1993. Unlike the South East Asian Countries, the momentum of the initial compel for good governance in India drew closer with the first glow of economic reforms in the country which began in 1990s. This has brought
with a series of corporate scandals. It instigated with a most famous the “Harshad Mehta Scam” involving a league of bull players in the stock market. The new regime of greater disclosure and transparency was wet in 1992 with the emergence of Securities and Exchange Board of India (SEBI) as an independent market regulator. The gradual empowerment of SEBI since then has played a crucial role in the establishment of basic rules of corporate governance in India.

Since the time of the traditionally called joint stock company, the key features of a company have been ‘incorporation by legislation as a legal entity’ and ‘separate from its owners’ (known as shareholders who have contributed their money in the form of share capital of the company). Other main features of the modern company are listed as under.

1. Incorporated Association,
2. Artificial Legal Entity,
3. Separation of Ownership and Management,
4. Limited Liability of its Shareholders,
5. Ownership Transferable,
6. Unbounded Ownership Scattered Globally,
7. Transparent and Consistent Existence

The segregation of the Indian companies may be broadly made amongst major two categories viz Private and Public Company. Both the categories have varied set of characteristics contradicting with each other mostly. These start with the kind of ownership and promoters. In the case of private companies the promoters are closely held associates, while in the case of public companies the promoters are widely held and with no limits of shareholding to be owned by number of shareholders. In India, the number of maximum shareholders in a private company is 50. Contrasting to this, there are quite a few companies in India having more than a million shareholders. For example, Reliance Industries Ltd., Tata Group of companies, etc. Another distinction is drawn for the restriction on the transferability of the shares. In the case of Private Companies, usually, the pre-emption clause becomes the restriction of transferring the shares. Private Companies have the freedom to make the provision of restriction on transferability in their Articles of Association. Contrasting to this, the shares of the
Public Companies are freely tradable and transferable amongst the general public with no limit on the maximum number of shareholders. In this way, the Private Companies have more freedom to have their own circumference on transferability of their shares. The public companies are further subcategorized as listed companies and unlisted companies. Listed public companies are those which have drawn their securities listed in at least one stock exchange of the country. That is how the listed public companies are bound to comply with the norms of the security market regulators – SEBI in India, SEC in U.S.A. and Financial Reporting Authority (FRA) in U.K. Whereas, the unlisted public companies have a slighter public impact and interaction. Though it is a public limited company because of its unlisted status, its shares are not freely traded amongst the open public. This ascertains a key quality about all public companies that is that “All Listed Companies are necessarily Public Companies, but all Public Companies are not necessarily Listed Companies”.

As far as the ownership patterns of these companies is concerned, another dimension of categorizing them is as widely held companies and closely held companies. Most of the listed public companies in India fall under the former category, whose shareholding is widely scattered amongst many individuals and institutions investors. While, most of the unlisted public companies as well as all private companies fall under the latter category as the number of shareholders of these companies are limited and constrained among very few investors. However, as far as the listed companies in India are concerned, most of them are closely held as family held companies. Even in most of the Asian jurisdiction, quite prevalent shareholding of listed companies lies with a single family, though they are the listed companies. In these kinds of companies the separation of ownership and management is less visible as more often family members and their close associates act as the managers and directors as well. This may leads towards the expropriation of the profit and broadly the whole interest of minority shareholders. Further more precisely, this is the state of affairs to concentrate more on the corporate governance issues.

As far as the wideness and size of the companies are concern, one more dimension of categorizing them is as standalone companies and group companies. Here the standalone companies are solo in existence and connection with any other companies. They have neither ownership connection in any directions with other companies nor
having any affiliation with them. Conversely, the group companies may be subcategorized among Pyramid Companies, Chain Companies and Network Companies. In India, the Pyramid structures of the companies are widely prevalent among the family and nonfamily groups those own companies incorporated within India as well as in many other foreign countries. Pyramid companies may be either of private or as public companies. In this subcategory, the company holding the position at the top of the pyramid that controls many other companies is known as Holding Company. While these other companies controlled by the holding companies are known as subsidiary companies. Many family companies in India have gloated number of subsidiary companies in which control is exercised through holding company. The most appropriate example of Indian company under this subcategory is the Tata Group of Companies. The other two subcategories of the companies i.e. chain and network companies are more prevalent in the other Asian subcontinental and continent European as well as in Japan and South Korea respectively.

1.3 Different Aspects & Theories of Corporate Governance:
Governance means ascendancy, power, authority, domination and control. These all features of governance are well applied in the decision making process and implementation of the decisions in any organization be it social, political, commercial, non-commercial, government, nongovernment, local, national, international. The concept of governance exists since the existence of human civilization. Therefore, wherever the human civilization involve in the activities for any outcomes for themselves, the governance of the whole activities comes into picture. When it is about governing any corporation’s activities, it is known as corporate governance.

In Indian context, Corporate Governance is very recent field of governing a firm or company which has been practiced over its owners and management simultaneously. “Corporate Governance is the system by which companies are directed and controlled by the management in the best interest of the shareholders and others ensuring greater transparency and better and timely financial reporting. The Board of Directors is responsible for governance of their companies.” Adam Smith had written in his seminal work got very famous as ‘Wealth of Nation’, “The directors of such companies, however, being managers of other peoples’ money than of their own, it
cannot well be expected that they should watch over it with the same anxious vigilance with which the partners in a private copartner frequently watch over their own.” Clifford C. Nelson, President of American Assembly once noted, “Corporate Governance is a fancy term for the various influences that determine what a company does and does not do or should and should not do.” Corporate governance is concerned with ways in which all parties interested in the well-being of the firm (the stakeholders) attempt to ensure that managers and other insiders take measures or adopt mechanisms that safeguard the interests of the stakeholders. Such measures are necessitated by the separation of ownership from management, an increasingly vital feature of the modern firm. A typical firm is characterized by numerous owners having no management function, and managers with no equity interest in the firm. Shareholders, or owners of equity, are generally large in number, and an average shareholder controls a minute proportion of the shares of the firm. This gives rise to the tendency for such a shareholder to take no interest in the monitoring of managers, who, left to themselves, may pursue interests different from those of the owners of equity. For example, the managers might take steps to increase the size of the firm and, often, their pay, although that may not necessarily raise the firm’s profit, the major concern of the shareholder.

Corporate Governance concerns to the problems that arise from separation of Ownership and Control / Management of the modern firms. Corporate Governance deals with the ways in which Suppliers of Finance to the Corporations assure themselves of getting a return on their investment. How do the Suppliers of Finance get managers to return some profit? How do they make sure that managers don not steal their capital? How do they make sure that the managers will increase the valuation of the corporation in which they have invested their finance? Enough law exists, but corporate governance is considered as one of the important instrument for investors’ protection and was rated high in the priority on the SEBI’s agenda for investors’ protection. Corporate Governance focuses on internal structure & rules of Board of Directors, Creation of Independent Audit Committee, Rules of Information Disclosure to the Share Holders & Creditors, and Overall Control of Management. The below exhibit rightly elaborates the ideal shape of a firm having the trivet foundation of a modern firm.
Here, the Shareholders and other stakeholders along with the suppliers of all resources have the major concern of getting returns or rewards of their investments in either of the forms. Whereby, the board of directors and the auditors, elected, selected and appointed by the shareholders, of the firms is primarily responsible to discharge their duties towards achieving these primary concerns of all shareholders and stakeholders. The board of directors of the firm appoints and supervises the management of their firm to execute these duties and tasks on behalf of them. The board is also responsible to report time to time about the business functioning and operation to the shareholders and other concern stakeholders of the firm. Corporate Governance, is thus, about, “maintaining appropriate balance of accounting and responsibilities between these three key players of the firm”. Thus practicing Corporate Governance establishes the relationship among various participants of the firm who jointly determines the direction and performance of the firm. The need of Corporate Governance arises because of two major changes over the past scenario: variety of stakes in a modern corporation, apart from the stake of the legal equity holders, and thanks to capital markets, major diversification of the equity capital leading to ever larger distance between the owners of capital and the managers. This has extended the requirements of practicing Corporate Governance with other reasons listed out as under.

- The decline of banking and the rise of the institutional investor,
- Increasing power and size of enterprises,
- Working of the economic system,
- Enterprises spreading Activities, Offices and Employees in dozens of countries,
- Shareholders scattered across the world,
- Corporate ownership and control not uniform in emerging markets and developed capital markets
- Emerging markets are dominated by “family enterprises”

Corporate Governance has been defined formally by some of the institutions and scholars in the following terms.

The Cadbury Committee of the United Kingdom defines Corporate Governance as, “The system by which companies are directed and controlled”.

According to the Organization of Economic Cooperation and Development (OECD), “Corporate Governance refers to the private and public institutions, including laws, regulations and accepted business practices, which together govern the relationship in a market economy, between corporate managers and entrepreneurs (Corporate Insiders) on one hand, and those who invest resources in corporations, on the other hand”.

Shleifer and Vishney (1997) define Corporate Governance as, “the ways in which suppliers of finance to corporations assure themselves of getting a return on their investment”. This conception is purely from the market-driven economies. However, this distinguish from the concepts of Corporate Governance prevails in the Japan and majority of European Countries. In these parts of the world, Corporate Governance signifies on creation of values for all stakeholders of the firm and their interests are affected by the decisions of the business operation.

Thus in the modern corporations, Corporate governance holds out the organism of structures, rights, responsibilities, duties, and obligations by and to the varied stakeholders of them by which corporations are directed and controlled. The governance mechanism specifies the distribution of rights and responsibilities among different participants in the corporation. These are the board of directors, managers,
shareholders, creditors, auditors, regulators, and other stakeholders. Corporate Governance also specifies the rules and procedures for making decisions in corporate affairs and their objectives are pursued through this mechanism, rules and procedures only; while reflecting the context of the social, regulatory and market environment. Governance aligns the interests among the stakeholders.

Above denotations about the Corporate Governance create contradictions amongst the interests of different people whose stake is there in the firms. This gives rise to assorted theories of the Corporate Governance.

1.3.1 Agency / Shareholders Theory:
The Agency Theory, in general, exists in the society in many walks of life where one party is being paid by another to get something to be done, whether in formal employment or a negotiated deal such as getting a car repaired or paying for household jobs. In the case of car repairing job, the car owner (the principal) wondering whether his car mechanic (the agent) is recommending expensive parts to be replaced because it is truly necessary for the car’s well maintained and good running, or because it will generate income for the car mechanic. The Agency Theory is based on the fundamental problem of separation of ownership and management of the firm. Financial economists have long been concerned with ways to address this problem, which arises from the incongruence of the interests of the equity owners (principal) and managers (agents), and have conducted significant research towards resolving it. The literature emanating from such efforts has grown, and much of the econometric evidence has been built on the theoretical works of Ross (1973), Jensen and Meckling (1976), and Fama (1980).

At the initial levels of the development of the agency theory, especially as it relates to the firm, concern seemed to focus more on the relationship between the management and shareholders than between them and other categories of stakeholders. Here, the shareholders, as principal owners of the firm, appoint the managers to achieve the objectives set by owners. It does not coincide every time, with the objectives of managers. Such divergence in the set of objectives between owners and managers is referred as the ‘agency problem’, which may lead the firm towards function for the
self-interest of controlling party i.e. the managers. This theory is also known as Shareholders Theory only because of the crux of managing the resources of the firm, by the managers, primarily for the objectives of the shareholders. Jensen and Meckling (1976) and Fama and Jensen (1983) have delineated Agency Theory as contractual theory of the firm wherein a firm is viewed as the nexus of contracts (written and unwritten) amongst different constituents (like Articles of Association and Memorandum of Association) of the modern firms that specifies the rolls, responsibilities, rights and accountabilities of the agents. Even-though, all such kinds of contracts exist between the owners and the management of the modern firms, many times, the managers exploit their control rights to pursue their own objectives and sometimes expropriate the funds of the firm in a varieties of practices for accomplishing their own objectives. This happens only because of their controlling and advantageous position than that of the shareholders in the moderns firms. To overcome this conflict and safeguard the shareholders’ objectives, the agency theory has prescribed certain mechanisms listed as under.

- Auditing System to limit the self-interested managerial behaviors,
- Changes in organization system to limit the ability of managers to engage in the undesirable practices, and
- Various bonding assurances by the managers that such abuses do not take place.

The problem arises where the two parties have different interests and asymmetric information, such that the principal cannot directly ensure that the agent is always acting in the best interest of principal, particularly when activities that are useful to the principal are costly to the agent, and where elements of what the agent does are costly for the principal to observe. Therefore, wherever the interests of the management (agents) differ from those of the shareholders (principals), the agency problem occurs. In any case, the Agency Problems lead to affording the agency cost. The deviation from the principal's interest by the agent is called ‘agency cost’. The below exhibit elaborates the conflict of interest amongst the management (agents) and the shareholders (principals)
Exhibit 1.2: Conflict of Interest among Agents and Principals

Simultaneously, Zajac and Westphal (1996) draw closer into view that the structure of directors in the form of executives and nonexecutives to resolve the agency conflict is also challenged. As per their study, the behaviour of the board members is also likely to be shaped not merely on the basis of their being insiders or outsiders but by their background, life values, experience and deliberate skills. Thus, the agency theory has its promoters and disbelievers. La Porta (1999) and others, under their cross national research project, revealed and suggested that in the developing countries, the primary agency problem has been traditionally among majority and minority owners and not amongst the owners and managers. In this kind of countries, most of the companies have been controlled by very small dominant group of owners by playing their dual roles of owners as well as managers. Instead of managers, here the dominant owners influence and overlook the interest of minority shareholders. Simultaneously, many Japanese, German and Asian Countries’ firms are fewer affected by the agency problems due to the block holding culture by banks and larger business families. In such kind of firms and countries, the agency theory has very extraneous prevalence. This gives importance to further theories of Corporate Governance.

1.3.2 Stewardship Theory:

Stewardship Theory of Corporate Governance envisages the managers beyond the agents of shareholders as superior stewards of the company and hence they discharge their duties and responsibilities very dedicatedly and devotedly towards the
achievements of very high level of returns on the shareholders’ investment. Stewardship Theory substitutes and contradicts a little to the Agency Theory by reducing the agency problems and ultimately the conflict of interest among the owners and managers. This theory of Corporate Governance marks down the possible conflicts between the agents and the principals. This kind of approach of managers establishes a large set of objectives in the priority list for them to be achieved for the authority of their firm. This includes devotions, dedications, responsibilities, recognitions, belief and respect towards the owners of the firm. Thus this theory believes that the managers are primarily trustworthy and focus more on the significant value addition to their own personal reputation and market values. As per the stewardship theory, the managers’ attitude alienates from appropriation of the funds of their owners and aligns with maximizing their market values. Donaldson L. (1990) conveys about the Stewardship Theory as, “it argues that managers are inherently trustworthy and not prone to misappropriate the funds of the investors”. This infers to the main differentiation between these two theories laying in the suppositions of the managers and their outlooks about their roles and responsibilities towards the authorities or owners of their firm. Donaldson L. & J. H. Davis, through their study on ‘Stewardship Theory of Agency Theory’ (1991) divulge that the CEOs as stewards of the firms are proved to be more prudence and efficient, as far as the high performance of the firms are concerned. Through this empirical study, the company boards with the nonexecutive directors are proved to be noncompeting against those of executive directors influenced boards. They demonstrated and conferred that the facilitating and empowering structure of the management of corporate governance is more rewarding instead of the monitoring and controlling one.

Kay, John and Silberston (1995) declare the Stewardship Theory known as ‘Trusteeship Theory’ viewing the business firms as a lawful creature of very long run and the large corporations as the social institutions; those establish the trustworthiness amongst the owners and the managers of them. Intact of company laws in the most commonwealth countries, U.K. and India too emphasis on directors’ crucial duties of managing and controlling the assets of the firms in the directions of owners’ objectives and not the directors own interests. Beyond the financial gaining objectives, the directors and managers of the firm have to carry on the firms’
existence in an ever-lasing mode. The Stewardship Theory of Corporate Governance has following attributes as its base to cutout the agency theory problems.

- It is based on the alignment of self-interest with those of the principals’ as motivation for the managers,
- Sticking behaviorally to the objectives of the firm,
- Managers function as the catch–all to ensure no issue affecting the business and affairs of the firm.

At the outset, it is to conclude that both the agency and stewardship theories of the Corporate Governance challenge each other with different mindsets and approaches of the managers of firm. On one side the managers as agents behave individually, opportunistically and self-servingly while on the other side, the managers as stewards behave collectively, pro-organizationally and trustworthily. Agents get motivated by their own set of objectives while, stewards get motivated by the set objectives of their owners. The agents play their role to monitor and control while the stewards play the role to facilitate and empower. And like this way, the Agent – Principal relationship is based on the control function whereas, that of the Steward – Principal is based on the conviction function. This may be inferred and based on the different approaches and attitudes of the managers acting as either agent or steward being a separate personal characteristic and having been influenced by varied cultural background. This situation leads to exploration of other theories of Corporate Governance.

1.3.3 Stakeholder Theory:

The Stakeholder Theory approaches and identifies the groups of different people contributing and involving their resources to a corporation, those are known as stakeholders of a corporation. This theory describes and recommends methods by which management can give due regard to the interests of these groups. In short, it attempts to address the "Principle of Who or What Really Counts. Stakeholder theory is a theory of managing the organization ethically ensuring to address the morals and values towards all the concern group of people. Therefore, this theory is beyond the focus on the interest of management (agents) and the shareholders (principals) only. Stakeholder theory battles that over and above the principals and the management,
there are many other clusters of people engross and concern to the corporation, these include employees, customers, suppliers, trade associations & unions, legislative & regulatory bodies, institutional financiers, political parties, and society at large. Even competitors are sometimes counted as stakeholders - their status being derived from their capacity to affect the firm and it’s above listed other stakeholders. These varied stakeholders may be subcategorized under two major categories vise Internal Stakeholders and External Stakeholders. The below exhibit narrates the list of stakeholders falling under these subcategories.

Exhibit 1.3: Various Stakeholders of the Company

The **stakeholder theory** has of late captured the attention of researchers and a survey of literature on this aspect of corporate finance can be found in the works of John and Senbet (1998). According to this theory, the firm can be considered as a nexus of contracts between management on the one hand and employees, shareholders, creditors, government and all other stakeholders on the other. Thus, from the point of view of the stakeholder theory, concern should go beyond the traditional management–shareholder relationship to include all other stakeholders such as mentioned above. Empirical work in the area of corporate governance
has undergone a remarkable growth, founded mostly on the basis of management–shareholder conflict and to a lesser but increasing extent on the stakeholder theory. Despite the volume of empirical evidence, there has been no consensus on how to resolve the problem. The lack of consensus has produced a variety of ideas (or mechanisms) on how to deal with the problem of agency. The mechanisms we are concerned with in this study can be divided into five: striking a balance between outside and inside directors; promoting insider (i.e., managers and directors) shareholding; keeping the size of the board reasonably low; encouraging ownership concentration; and encouraging the firm to have a reasonable amount of leverage in the expectation that creditors might take on a monitoring role in the firm in order to protect their debt holdings.

Numerous researches and literatures have been developed and published on the stakeholder theory, but the major credit of emergence of this theory goes to R. Edward Freeman who is also known as the “Father of Stakeholder Theory”. His ‘Strategic Management: A Stakeholder Approach’ is broadly quoted in the meadow of Corporate Governance as being the keystones of Stakeholder Theory.

T. Donaldson and Preston (1995) argue that the theory has multiple distinct aspects that are mutually supportive: descriptive, instrumental, and normative. The descriptive approach is used in research to describe and explain the characteristics and behaviours of firms, including how companies are managed, how the board of directors considers corporate constituencies, the way that managers think about managing, and the nature of the firm itself. The instrumental approach uses empirical data to identify the connections that exist between the management of stakeholder groups and the achievement of corporate goals (most commonly profitability and efficiency goals). The normative approach, identified as the core of the theory by Donaldson and Preston, examines the function of the corporation and identifies the "moral or philosophical guidelines for the operation and management of the corporation." Since the publication of this article in 1995, it has served as a foundational reference for researchers in the field, having been cited over 1,100 times.
Mitchell, et al. derive a typology of stakeholders based on the attributes of power (the extent a party has means to impose its will in a relationship), legitimacy (socially accepted and expected structures or behaviors), and urgency (time sensitivity or criticality of the stakeholder’s claims). By examining the combination of these attributes in a binary manner, 8 types of stakeholders are derived along with their implications for the organization. Friedman and Miles explore the implications of contentious relationships between stakeholders and organizations by introducing compatible/incompatible interests and necessary/contingent connections as additional attributes with which to examine the configuration of these relationships. Robert Allen Phillips distinguishes between normatively legitimate stakeholders (those to whom an organization holds a moral obligation) and derivatively legitimate stakeholders (those whose stakeholder status is derived from their ability to affect the organization or its normatively legitimate stakeholders).

1.3.4 Enlightened Stakeholder Theory:

The stakeholder theory has undergone some refinements in the work of Jensen (2001), who presents what he terms the “enlightened stakeholder theory”. For him, the traditional stakeholder theory encourages managers to be servants of many masters, with no clear guidance whenever trade-offs (or indeed, conflicts) occur, as they often do. He argues that the absence of any criterion for choice in cases of trade-offs (or conflicts) tends to give managers some discretionary powers to serve the master of their own choice. As we will see in a subsequent section, Jensen proposes a single criterion – addition to the long-term value of the firm – for managers to pursue so that the interests of all key stakeholders can be served. This is based on the idea that changes in the long-term value of the firm would be difficult to materialize if the interest of a key stakeholder were not protected.

1.3.5 Sociological Theory:

Since, the firms has got involvements of many stakeholders, the society at large becomes the most significant stakeholder of the firms. Above discussed all theories of the corporate governance are powerful tools and provide important insights in
examining the impact of ownership and other criterions on firm performance, they endure from the severe constraint of excluding the examination of the social context within which the firm’s activities are implanted. The sociological approach to the Corporate Governance has been emerged in the recent decades of 21st century. This theory focuses largely on board composition and more importantly on the implications for power and wealth distribution in the entire society. Beyond the enlightened stakeholder theory, under the sociological theory of Corporate Governance, the problem of interlocking directorships and the concentration of directorships in the hands of a privileged class are viewed as major challenges to equity and social progress. Under this theory, board composition, financial reporting, disclosure and auditing are necessary mechanisms to promote equity and fairness in the society. The norms of International Financial Reporting Standards (IFRS) have also been introduced very recently those become required to be complied with as a part of sociological theory as far as the internationalization of the firm is concerned.

1.4 Governance of an Indian Firm:
The Industrial enlargement and incorporation of giant business corporations in India took place only after its independence in 1947. Before independence, most of the stakeholders of Indian Corporations had been suffered by malpractices and seize of most of the natural resources by then ruling Europeans controllers. Post-independence, throughout 20th century, the fraudulent dominance practice with the characteristics of unscrupulous behaviors of the Indian bureaucrats and politicians had cultivated the unethical and outrageous culture amongst the Indian corporations and giant firms. This has led them to extend negligible consideration towards timeless human and organizational values in dealing with their employees, shareholders and customers. Due to such kind of cultural developments in the Indian firms and business corporations, their management has kept themselves above accountability for their offenses, and encouraged towards indulging in more unethical practices of these firms. Most of the states and nation owned government corporations, having monopolistic position in certain natural products and services, have conceded and levied the cost of their non-governance on their vulnerable Indian customers and consumers. While the private giant firms and corporations excluding a few, enjoying
large domestic economic position, have indulged their customers and consumers in all possible ways of unethical practice and influenced the state and central regulators as far as their compliances are concerned. During last decade of the 20th century, large number of private business firms’ owners have ruined their business and seized the investments of their shareholders. Many recorded scams committed in number of large privately owned Indian firms during this phase indicate the nature and extent of corporate mis-governance that exists amongst their governance practice.

An Indian company is incorporated as an artificial person having its own seal that creates its lawful existence. Being its artificial lawful existence, it may require representatives to be run by and lead towards achieving its set of objectives laid down in many lawful contracts like memorandum of association. This is the primary reason of having the board of directors in any registered firm. Company Legislations of most of the commonwealth countries including India ascertain statutorily to have the board of directors for running the companies’ business and achieving their objectives. The board of directors is a group of persons known as representatives of the firm because their selection is done by the shareholders of the firm and they have to act for the interest of the shareholders. In Germany and some of the Continental European countries, the firms have two tier board of directors vise supervisory board and management board. The board of directors is, generally, elected by the shareholders during the annual general meeting of the firm. Being the scattered and numerous in natures, another reason to have the board of directors, the shareholders of the firm are not in a position to undertake and participate in the firm’s management and day to day operations and to run it.

The elected board of directors, then after, appoints, monitor, supervise and evaluate the senior executives and managers including chief executive officers (CEO), chief operating officers (COO), presidents, or whatsoever it is called to undertake the day to day operations of the firm and run the firm under their supervision and directions. The board of directors, thus, becomes the governing body of the firm, while the managers become the executive body of the firm. Wherein, the governance of the firm is bested in the hands of this body having not a single person known as CEO, COO, or President but in multiples hands of the board members. The board is empowered and responsible to set the objectives, rules, regulations, procedures, policies, and strategies
of the firm and accordingly get the things done by the managers or executives of the firm. With this intention, they enjoy the ultimate decision making authority in the firm too. They derive these entire governing holds through the articles of association, another lawful contract being entered into by the firm. For this reasons, the board is held liable too, for the consequences of the firm’s actions and reactions. The board, moderately, gets the authority only through its formal meetings and by passing resolutions during these meetings. While the senior executives and managers of the firm are responsible to execute and operate day to day functioning of the firm. They are accountable to align their performance and report for their outcomes with that of the board’s procedures, policies, strategies and objectives. They are regularly got monitored and supervised by the board for the same. This manifestation establishes the crux of the firms having three layers of owners, governors, and managers of the firms. Below exhibit elaborate this chain of relationship more precisely.

Exhibit 1.4: Governance Relationship in a typical Indian Firm

From the above exhibit, it is inferred very clearly that the governance and management of a firm is undertaken on behalf of and primarily for the shareholders of the firm. While being the controller of the firm by ownership, the shareholders concede the major controlling norms, as far as the business operations and functioning are concerned, to the board and the management of the firm only. This separates the ownerships and control of the firm’s business and later on it gives birth to the agency
problem that has been discussed earlier. The Indian Firms have not been escaped from this governance issue since their inception. The recorded scams and scandals in Indian firms starting from 1992’s big bull ‘Harshad Mehta to Ketan Parek and further to the Satyam Fiasco has been the upshots of the governance problems in the Indian Firms. These circumstances lead further to explore the study on many other consequences being occurred due to such kind of issues of the governance of Indian Firms. Many researchers in India have already undertaken different studies on the Corporate Governance and its issues and impacts on the firms’ financial performance of Indian Firms till now. Dr. Parmjit Kaur & Dr. Suveera Gill (2008) reveled, in their study on ‘Effects of Ownership Structure on Corporate Governance and Performance’ that, the ownership concentration does not have a significant impact on performance. They also derived the mixed influence of board independence on corporate performance. Their results of board size categories revealed an inverse relationship between board size and corporate performance. Another study of selected family owner Indian firms undertaken by Jiban Mukhopadhyay et al (2012) has concluded that Corporate Governance has a definite impact on financial performance of family managed Indian Firms. There are many such kinds of detailed researches have been initiated and revealed the mixed outcomes about the Indian Corporate Governance practices.

Rejie George Pallathitta (2005) reveals that as far as directors and their relatives’ shareholding is concerned, it has mixed impacted on few Indian Firms’ financial performance under his study. He also reached to the conclusions that in a longer term as the government progressively relinquish control over domestic financial institutions; Indian private institutional investors could gain in prominence and skill. Lal C. Chugh et al (2010), find that board size creates better opportunities performance. An excessively autonomous board (high proportion of independent directors) lowers performance. Their study also finds the situation of CEO synergies with the financial performance. Palanisamy Saravanan Et Al (2012), under their study on the corporate governance and firms’ performance of Indian manufacturing firms, found that the firm value is significantly affected by the corporate governance variables.

It is eccentric but factual that the primary initiative for improved corporate governance in India took place from the more progressive listed firms and moreover
from an industry association. This has been relatively diverse from those in US and Great Britain, wherein, the corporate governance has been driven not only by the group of shareholders but also by many activist funds and self-regulatory bodies within capital and security markets. This has also been dissimilar from East Asian and Southeast countries’ firms, wherein, the good corporate governance was imposed by the IMF and the World Bank in the wake of the financial collapse of 1997 – 98. Before one year of this time period only, Indian firms boarded for corporate governance movement where there was no major financial crisis or problems of balance of payments prevailed. In 1997, it is the Confederation of Indian Industries (CII) who initiated very first time, the Corporate Governance Movements and given their code of conducts for corporate governance in India. Till 200, almost 30 large listed firms holding for over 25 percent of Indian market capitalization voluntarily adopted the codes. Before that, by 1999, the Securities and Exchange Board of India (SEBI) released its act and set up a committee headed by Kumar Mangalam Birla to mandate international standards of corporate governance for the listed firms. By the time of April, 2003; each and every listed firms joined and adopted the SEBI codes of corporate governance. This all has happened only with the changes in corporate mindset brought about by economic liberalization and competition of the 1990s.

1.5 Boards & Committees in Indian Firms:
Directors appointed by the voting process in the annual general meeting become the official and legal agents of the firm to direct and manage the conducts and affairs of its business. Since the firm being the artificial person many not act by itself to carry on its business affairs, the directors act on behalf of the company and ultimately the shareholders. This holds all kinds of the legal liabilities with the firm as an artificial person only and not any of the directors become liable for any default or breach in the firm. The directors are responsible and accountable for maintaining the assets and resources of the firm in a good and working conditions and controlling their usages in the wealth generation for the firm and its shareholders. That is how; sometimes they are also referred as trustees of the firm as they plunk in the fiduciary capacity towards the firm. As trustees of the firm, they are liable to execute their tasks and exercise their powers dedicatedly for the benefit of the firm and its shareholders. For any
misconduct or misleading of the assigned powers to them, they could be rendered liable as trustees. Anderson, C.A. and R.N. Anthony (1986), opine that, “Directors are the persons selected to manage the affairs of the company for the benefit of shareholders. It is an office of trust, which it is their duty to perform fully and entirely”. Out of these elected directors, various committees are formed to facilitate effective monitoring of companies by focusing on corporate issues in detail.

1.5.1 Board of Directors:
The directors of a firm collectively called as ‘board of directors’ or just as the ‘board’ is the governing body of a company to look-after the day to day operations and business functioning of the company and run the company on behalf of its shareholders. The legal scaffolds of the country elaborate the roles, functions, responsibilities and the authority of the board. Director is the member of this board duly elected by the shareholders in the annual general meeting of the firm. The person once becoming the member of the board of the firm, by whatever name called, may be termed as director in the lawful meaning. The legislations in India and many other countries define the meaning of directors as same for different types of the directors of the firm. These directors may be of one of the kinds of Executive Directors, Non-executive Directors, Independent Directors, Lead Independent Directors, Nominee Directors, Additional Directors, Alternative Directors, Shadow Directors, or a De Facto Directors. Perceptibly, the appointments and tenure of these all kinds of directors differ from each other, but their acts and roles contribute to the governance of the firm in any customs. At the time of incorporating the firm, its promoters must have appointed the board of directors through their contractual documents of Memorandum of Association and Articles of Association. They are the first directors of the firm and later on through the first annual general meeting, by passing a resolution with majority; the shareholders of the firm may elect different board. All these directors are appointed on the rotation to be retiring with the ratio of one third every year.
In most of the Asian countries especially in China and India, the family managed closely held companies nominate and appoint directors on the strength of their holdings in the firms. Till recently, the boards of these firms used to be filled with family members or closely associated friends or family circles. A large change in the composition of the boards of such kind of family owned and managed firms is evident now with the induction of independent directors to comply with the corporate governance codes. The practice of appointing directors by a straight majority of votes of the shareholders is of very recent emergence and also has very less pace. In this practice, the major drawback is of monopolizing the entire directorship by a single shareholder or a group of shareholders holding more than 51 percent or more shares in the firm. This leads to the confronting situation with no representative of the minority shareholders as the director on board. Section 265 of the Indian Companies Act, 1956 provides the option to adopt the system of proportional representation of the directors by various shareholders group.

The size of the board varies from country to country as well as within the country among the companies worldwide. The countries like Japan and South Korea have very large boards of 30 ups directors on the boards of their firms, whereas, the firms in the most of the other first world countries like U.K., Canada, U.S.A., etc. incline to have a small board of 8 to 15 directors. In India, firms have reasonably law numbers of the directors on the boards of its firms ranging from 6 to 18. The size of the board has much influence on the firm’s performance, the behavior of the directors, group dynamics of the board, etc. The size of the board of the firms in any country relies on legal framework of the country, codes of the corporate governance, norms regulatory bodies of the firms, scale of operations of the firm. The board size infers the questions like, is the size important? What is the ideal size of the board? Does the size influence the firm’s performance?, etc. Many detailed researches and studies have been undertaken on these all areas of the board of the firms. As far as the structure of the board is concerned, the composition of the board of directors may take one of the three forms: all executive directors, all non-executive directors, and a matrix of both of these. Most of the private and family owned firms prefer to have most of the executive directors on its board that also includes few of their promoters acting as managers and executives. Most of the non-profit making firms as well as many of the
state or national government undertakings comprise of the non-executive directors entirely. Between these two extremes of the board structure, gigantic digits of firms exist in many countries that have the mix of executive and non-executive directors on their board. Many of these mixed components of the board is also comprised with the recent category of the directors known as Independent Directors. This category is expected to curtail the conflict of interest between the shareholders and the other directors as executives of the firm. Cadbury, Sir Adrian (2002) concludes that there is general consensus in the conceptual literature that effective boards comprise of higher proportions of independent directors. Many researches on this area also have been undertaken and reached to the conclusion that the firms controlled by business families in the Asian Countries like China, Malaysia, India, Thailand, etc. have more importance of the independent directors on their boards. Since last two decades of the 20th century, large listed companies in many developed countries like U.S.A., and U.K. have increasingly altered into a board having majority of non-executive directors with independent directors among them.

As far as the leading of the board team is concerned, he is the person known as the chairman of the board. S/he is officially elected by the members of the board on the base of voting process in the board meeting. The chairman of the board is primarily responsible for running the board functions very slickly and interacting with the Chief Executive Officer (CEO) or Chief Operating Officer (COO). S/he has to ensure through CEO or COO or CFO that the board meets regularly and is able to take the significant decisions with adequate information provided to them timely. S/he also has to ensure that the shareholders and other financiers of the firm shall get the financial and other reports quarterly, half yearly and annually as applicable. In many Asian Countries like Japan and Korea, the CEO or Managing Director leads the management of the firms. While in western countries, the CEO or COO of the board becomes the chairman of the board of firms. This situation escorts to face the conflict of interest as well as independent oversight of the management. Many researchers have undertaken detailed studies on this issue of corporate governance having whether the role of chairman and COE should be separate of combined within one person? Many of them have reached to the conclusion that if chairman and COE of the firm is the same person, it becomes more difficult to manage the board and lead
their interest aligning with those of the firms and ultimately of shareholders of the firms. Holding the Chairmanship and CEO position by a single person is known as duality concept. Kesner, I.F. and R.B. Johnson (1990) prove that duality concept of corporate governance provides integrated firm leadership and removers internal or external uncertainty concerning who is accountable for firm progressions and outcomes. They infer that the duality of the chairman and COE has greater commitment to the firm than a separate chairman from COE.

1.5.2 Board Committees:
The directors of the board are nominated as members of different sub-boards known as board committees. This is a recent trend to have such kinds of committees of the boards which are more often standing and empowered to make relevant decisions and required to report to the board of directors. The committees are formed for the temporary terms only to make certain investigation or recommendations and report to the board. Through various committees, the board facilitates effective functioning and monitoring day to day corporate instructions, issues information. The corporate governance guidelines and mechanism of most of the world economies have mandated, through their companies law board, to have three principal committees to be formed within the board members. These are Audit Committee, Remuneration Committee and Nomination Committee. As their names suggest, these are known as standing committees of the board which are formed for the specific purpose of firm’s auditing, board members’ remuneration and board members’ nomination determination.

Audit Committee is formed to review financial implications and the scope of audit before the actual audit is undertaken. It also reviews the post audit reports as well as the financial management’s objectives of financing, investment and dividend policy decisions. Audit committee performs the role of intermediary in-between the internal auditors and the statutory auditors. Internal auditors have to report to this committee about any significant findings, discrepancies, irregularities in the financial reporting of the firm. Whereas, statutory auditors have to report to this committee about any deviation from norms and accounting manipulations happened due to lack of
information submission as well as appropriate and commensurate internal control system to be set by the management of the firm. The audit committee is entitled to meet regularly to the internal and statutory auditors to examine and appraise the audit plans and ascertain the effective controlling system to be implemented. Audit committee investigates and take appropriate measures, if finds any considerable evasion, by the management, with any stakeholders of the firm. It also supports to the board to understand the financial information and implication about the financial decision makings of the firm. Thus, this committee builds the bridge between the board of directors and the auditors.

The audit committee meets at least once in every quarter and strengthens itself to discharge its duties as intermediary as far as firm’s auditing as well financial and accounting regulations are concern. In 1970s, the U.S.A. firms have invented first to have the most important subcommittee of the board of the directors known as audit committee. It was, by then, envisaged as an interface between the external auditors and the board of directors. Later than almost half century, today this committee has gained the most significance to overcome the financial reporting omission in most of the world economies starting from U.S.A. till India and Singapore as well as Malaysia too. The role of audit committee, now, has been expanded from the pre audit and post audit review to the integration of financial reporting, lapse of risk management, foreign currency and balance of interest rates, and compliance with the corporate governance parameters.

**Remuneration Committee** is formed to recommend to the board of directors on the remuneration or compensation to be offered to the directors mainly the executive directors who contribute to the day to day functioning of the firm. Around the world’s corporate fraternity, disproportionate remuneration offering to their executive directors have been most concerned governance issue among those corporate. This governance suspicions could be handled well by the intervention by formation of official subcommittee consisting wholly or majorly of independent directors of the board. Remuneration committee designs the compensation package of the directors of the board in such a way that ensures compliance of governance regulations along with the affirmation of availability of sustainable, motivated and efficient executives on the board. The compensation package includes salary, special fees, stock options,
perquisites and pension benefits for the executive directors and CEO as well as other senior executives of the firm. Beyond this, the role of committee includes recommendation on the post-retirement benefits, duration of the contract as well as the notice periods and termination payments, performance related schemes, assessment norms, etc.

The responsibilities of the remuneration committee exclude the nomination of any members on the board. As per the articles of association of the company, the executive members of the board determine the remuneration of the non-executive and other directors, if any. None of the directors or executives gets involved in their own remuneration structure designing process. For preventing the lucidity and equality in the remuneration structure determination process, most of the members of this committee comprise independent and non-executive directors only. In the case of chairman of the firm being the independent or non-executive, s/he may become the member of the remuneration committee and not the chairman of this committee too. This committee may arrange their meeting at their convenience and as need arise.

**Nomination Committee** is formed to set the standards of nomination, screening and reviewing the probable directors of the board. Directors of the board are appointed and reappointed, usually during the annual general meeting of the shareholders by the voting process, but many times it happens to be practiced on the recommendations of the existing executive directors on the board of firm. Nomination committee, with transparent and fairly identification and recommendation of proposed directors, ceases the board becoming a homely alliance or quiescent body of closely associated persons. This committee is responsible for formulating the policy and procedure of recommendation, screening and reviewing the competent, skilled and upbeat persons as directors who would initiate, innovate and improve the firm’s functioning and providing their best to the growth of the firm. The committee would consider various criteria of identifying, and selecting the directors including the appropriate professional knowledge, industry expertise, relevant educational background, etc. Thus the capabilities and attributes needed to become the board members are suggested by the nomination committee. Nomination committee is also empowered to give the recommendation on removal of any existing members on the board. It is also
entitled to assist the board chair in identifying suitable person for the position of CEO or COO of the firm, as when it is required to be replaced.

The nomination committee comprises of two to three members usually all being the non-executive or independent directors of the board. The chairperson of this subcommittee is preferred to be the chairman of the firm, if s/he is the independent director. There is no prefixed interval of meeting this committee during the year. As and when the members of this subcommittee consider it as required or suitable, they arrange a formal meeting. For discharging their responsibilities, they often meet the senior employees or executives of the firm or may sometimes consult the external stakeholders, if any they deem feet to take any suggestion or inputs from. Nomination committee reports to the existing board about their observation, identification and other criteria about the proposed candidate to be taken as members of the board. The chairman of the nomination committee regularly attends the AGM of the firm and takes the suggestions and inputs from the shareholders about their view on appointing or disappointing any members of the board. At the outset, nomination committee has to ensure that the firm has a board of sufficient size with the appropriate balance of skills set and expertise along with the relevant experience to convene the firm’s present and future needs of the growth and expansion. To form the subcommittee like nomination is very popular and prevalent trend among the corporate undertakings across the global economies.

Among the above all three committees, the nomination committee stumble on less acceptance from the existing board and its members, because of its interference and intervention in the construction of the board. This is also because of the entire power of selecting and appointing the directors are exerted to the shareholders. It is desirable for the nomination committee to work closely with the remuneration committee to exercise their power together and perform their tasks of constructing the most efficient board. The board of directors is entitled to form such kinds of subcommittees for the smooth and effective functioning of the firm’s business as well as discharging their duties well and in a required manner. All such kinds of subcommittees must be independent in symphony as well as move toward their responsibilities and authority as well as power of execution of their tasks.
1.6 Models of Corporate Governance:

The corporate governance models define various systems of governing the corporate along several dimensions. The significant dimensions are ownership structure, shareholding patterns, capital market outlines and banks and institutional intermediaries’ financing styles. The corporate governance models are also inclined by other criteria like disclosure system, incentive schemes, legislative strength, workers participation, and pace of takeover market. Mc Kinsey & Company’s report (2001) suggested major two models known as ‘Market Model’ and ‘Control Model’ under which the corporate governance system of the entire world economies could be segregated and covered. The former one is prevailed and accepted more commonly in the U.S.A., the U.K., Canada and Australia. While, the latter one is prevailed moreover in the Latin America, European Continental Countries and Asian Countries.

Beyond these models suggested by Mc Kinsey’s report, the prevailing model of corporate governance in Germany and Japan is known as ‘Bank-oriented Model’. Due to the large persuade of Family owned business model, in many developing countries like Thailand, India, Hong Kong, Malaysia, and other Middle East Countries, the mix model of corporate governance is accepted. The large family ownership holding pattern in these countries along with the strong holt and relationship with the bankers lead them to have the hybrid model of corporate governance practice. Thus, the entire corporate world economies may be separated under four corporate governance models elaborated as under.

1.6.1 The Anglo American Model:

The Anglo American Model of corporate governance is developed on the bases of well-established stock market; broaden individual shareholders and the joint board of Insider and outside directors. This is also known as ‘Unitary Board Model’ or ‘Anglo-Saxon Model’, because of its prevailing in the U.S.A., U.K., Canada, Australia and many commonwealth countries like India as well as its characteristics of having single board comprising with both executive and none-executive directors respectively. This neglects the presence of Independent Directors on the board. Here the inside directors represent as executive directors and outside directors as the non-executive directors of
the board. The corporate fraternity of these economies is surrounded by well market capitalism with substantial degree of liquidity and depth of the stock market. This minimizes the trade unions’ influence as the model doesn’t allow the labours to participate in the strategic decision making as well as exercising on the board of directors formation. The top most firms of these countries are listed on the stock markets and the market capitalization rate is also very high in these countries.

Another major characteristic of this model is dispersed shareholding pattern. La Porta et al (1999) shows, in his formal study on this matter that the equity shares of typical Anglo-Saxon Model firms are widely dispersed. The median size of the largest voting league in the U.S.A. is less than 5 percent and that in U.K. is almost 10 percent. This weakens the shareholders influence on the management and leads towards the precise separation of ownership and management. In Anglo American Model, the sound legislation and systematic regulatory compliance mechanism endow with the shareholders protection.

1.6.2 The German Model:
The German Model of corporate governance is developed on the bases of less established financial market, closely held large shareholding bloc and dual boards’ layer. This is also known as ‘Continental Europe Model’ or ‘Two-tier Boar Model’, because of its prevailing in the Germany, Holland, Switzerland, Netherlands and France as well as its characteristics of having two boards, one is supervisory board and the second is executive board respectively. The corporate fraternity of these economies is surrounded by less market capitalism with substantial degree of banks dominance and large bloc of closely held shareholdings. This model instigates the employees’ and labors’ influence by participating in the management decision making as well as exercising on the board of directors formation through their unions. In this model, the firms enjoy the cross shareholdings among themselves and extensive role of banks in their financing.

The half of the supervisory board members are elected by the shareholders and the supervisory board then appoint full time managers and other members on the executive board of the firm. In this pattern, the executive board of the firm enjoys the
high level of autonomy in the managing of the firm while the supervisory board performs the role of decision making authority through the shareholders influence. This two-tier board system directs the business functioning with the more societal-oriented style. In compare to Anglo–American Model, this model exerts the low capitalization ratio to GDP, less number of listed equities in the stock market, illiquidity of the funds and more floated banking systems. In Germany as well Continental Europe, most of the listed and many unlisted firms have the owners’ shareholding on a very larger side of 50 percent or more. This makes the other shareholders very weak in the controlling of the firms’ business. In such kind of model, the banks habitually mingle a number of roles namely, supply of equity as well as debt capital, board representation, exercising veto power, etc.

1.6.3 The Japanese Model:

The Japanese Model of corporate governance is developed on the bases of cultural relationships seen in the Japanese keiretsu network of most of the banks, cross shareholdings amongst a small number of dominant groups and the board of directors and the president being appointed by shareholders and the main banks. This is also known as ‘Zaibatsu’, that is a totally integrated group engaged in manufacturing, logistics & supply chain and trade & finance across a wide range of business as well as it is characterized with having retired government officers to be placed as directors. This ensures the presence of effective governance practices and policies to be implemented and controlled by government and its bureaucrats. Here the shareholders appoint insider directors as executive directors and main banks offer the board membership to their executives as outside directors of the board. Thus the corporate fraternity of these economies is surrounded by a relationship model based on supports of banks and government. This model also nurtures the board membership to be offered to senior managers and executives of the firm. This enlarges the employees’ participation in the firm’s governance and ensures the long term devotion and dedication of the employees.

Another major characteristic of this model is its being the ‘Network Model’. In the firms, under this network model, the boards surrender their entire authority to the
president of the company and he is vested with complete governance power. He then creates a personal relationship’s network with different business and other associates as well as government officials. This minimizes the shareholders influence on the management and leads towards building the precise and integrated social unit. In Japanese Model, the sound networking and contingency governance endow with the successful growth and market value maximization.

1.6.4 The Family – Based Model:

The Family – Based Model of corporate governance is developed on the bases of fragile stock market, broaden family dominant shareholders and the interlocking & family appointed directorship. This is also known as ‘Bloc – Holder Model’, because of its bulk of share capital is concentrated with a single family in majority of the firms of the East Asia, Middle East Countries, South America and many commonwealth countries like India. This raises conflict of interest between the controlling and the minority shareholders and also overlooks the protection of minority shareholders investment and interest. That is how, in this model, the agency problem of corporate governance is prevailed not amongst the principals – agents but between the principals – principals. Morck and Yeung (2003) point out that, ‘in family business group firms, the concern is that managers may act for the controlling family, but not for the shareholders in general’.

Another major characteristic of this model is nonexistence of separation of ownership and control, because of the controlling of the business is exercised mostly by the families directly or indirectly. It is said that the first generation initiate the businesses with the internal funds only. Later on they develop and grow their business with their instinct entrepreneurship skills and wealth creation generation attributes. These families have high regards and recognition in their economies and they fill the market mechanism monitoring gap. The biggest drawback of this model is uncertainty of replicating the entrepreneurship skills and wealth creation and sustaining tactic in the next generation of these families. Another drawback of this model is to inculcate south corporate governance practices and to manage the firms through the proficient management in the modern complex corporate world.
1.6.5 The Indian Model:

The Indian Model of corporate governance has been developed primarily on the bases of underdeveloped stock market, closely held shareholding pattern and the insiders’ directorship. The structure and operation of the Indian Firms have been aligned with that of German and Japanese Companies. This is because of its less transparent disclosure practice, insiders and interlocking bloc holdings and concentrated share holdings with a single family running business till the adoption of Liberalization, Privatization and Globalization in 1990s. Till this time, the mergers and takeovers are of the rare occurrence and the new capital issue market had also been underdeveloped. This again raised conflict of interest between the controlling and the minority shareholders and also overlooks the protection of minority shareholders investment and interest.

The Indian corporate have been governed by the company’s Act of 1956. Ever since 2000s, the corporate governance reforms have taken place in the Indian corporate which has started transformation among them and adopted habitually the Anglo – American corporate governance mechanism. As of 2000, as far as the legislatives mechanisms is concerned, Indian government through SEBI and industry association CII constituted various committees to review and revise corporate governance practices in the country and put forward measures for progression based on what has globally acknowledged as ‘best practices’. These committees are assorted from Task Force chaired by Rahul Bajaj (1998), Kumar Mangalam Birla Committee (2000), Naresh Chandra committee (2002) and Narayan Murthy Committee (2003) appointed by the SEBI. The recommendations of most of these committees are incredibly analogous to those of England Cadbury committee (1992) and America’s Sarbanes Oxley act (2002) in provisions of their approaches, advices and approvals concerning to the corporate governance mechanism and practicing good governance. Through this way, the Indian Firms has adopted external and internal mechanism especially in the realm or the legislative framework where Indian policy-makers have taken their nod from the U.K. and U.S. committees and recommendations and show a prototype transfer from German / Japanese Model to the Anglo – American Model of Corporate Governance.
These various governance mechanisms delineate a put together overall corporate control in each company law jurisdiction. These Models diverge on various aspects of corporate governance vise Ownership Structure, Board Composition, Shareholding & Financing Pattern, Stock Market, Chairmanship and CEO Prototype and Employees & Workers participations, etc. It is imperative to perceive the entire package of overall corporate governance. There has to be an integrated concord involving state legislation and authoritarian infrastructure, stock market regulation and corporate and self- regulation. Nonetheless, Corporate Governance practices are in a situation of transformation across the world and divulge signs of convergence.
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END OF CHAPTER - I