

Corporate Law and Corporate Governance: Relationship Study

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Abstract

The study of corporate governance is not complete without the deep understanding of corporate laws, company law and corporate law theories. Corporate governance is matter of discussion in present time by academics, business, regulators and lawyers especially after 1980 that resulted to collapse of large corporations and economic crisis in Asia. This research article deals about the relationship study between corporate law and corporate governance and attempts to answer why the study of one is not enough to understand another. It is about corporate power, accountability, transparency and direction about how the corporation is to be governed and by whom.

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Introduction

Anyone thinking of corporations in prima facie think of large companies or business entities established to carry out certain purpose including profit oriented companies, public and private companies, joint ventures, co-operative, partnership, not for profit organization, state owned corporate entities. The existence of such entities without any governing body cannot be imagined to execute or operate. Such bodies have the governing bodies with different names like council, committee, a board of governors.³

Business is the backbone of economics and dominant business form is company or corporations. It is important to discuss how the companies are governed because it is an all-important vehicles for allocating and efficiently employing capital in our society providing goods, services and revenue. In common sense, law of Business Corporation is structured by company law. So what about corporate law, corporate laws are of wide scope of companies that includes securities law, competition law, Intellectual Property law with corporate governance, share ownership, capital markets and business culture. The principal function of corporate law is to provide business enterprises with a legal form that possesses separate characteristics. These characters are widely available and user-friendly, corporate law enables entrepreneurs to transact easily through the medium of the corporate entity, and thus lowers the costs of conducting business. These corporations are born from the state company law and securities law. Constituting modern companies identifies separate characteristics as a separate legal personality, limited liability of owners and managers, shared ownership by capital investors capital, delegated management under the board structure and transferable share. At first, it is important to understand the corporations and relevant laws- (i) company Law defining legal standing of public, private held corporations, also defines liability of owners in private corporations. In case of public companies, the relationship between the board, shareholder, managers and other stakeholders. We see the separation of ownership from control in public held companies. Second financial market regulation that defines how to obtain capital for their operation and the relation with banks, equity, debt markets. It governs all the transactions in both public and private (iii) labour law defining how labour contract operate, the rights worker participation in governing body. Before beginning on corporate governance, it is important to understand what are the main goals of corporate law? Corporate Law regulating financial relationship and defines conflict among the participants in corporate entities. In law it also focuses on solving the interest of society as a whole. In broad

³R.I BOB TRICKER, CORPORATE GOVERNANCE: PRINCIPLES, POLICIES AND PRACTICE 4 (3rd ed. 2015).

sense it can be said all the entities having interest in activities of business entities and interest in their management and control. It includes owners, managers, customers and society. So there is conflict in law, to whom the corporation should serve, should it serve to shareholders who contribute their capital in the Corporation or managers, employee that operate business or say society to whom business entities benefit from the society. The main conflict in Corporate Law is separation of ownership from control that is to say the agency problem the conflict between shareholders, managers and employee or non-shareholders. Second the issue regarding to whom the corporation should serve either on maximization of shareholder return in general or in advancing overall social welfare.

It is universally understood that shareholders contribute capital to companies in widely held public companies. Shareholders elect board of directors and BOD elect managers. Now the Board gets power from shareholders to decide how to run the company in efficient manner as per the purpose of the company established. They make a valuable decisions leaving some rights to decide from shareholders. Managers act day to day operation of the company. It is now clear that there exists separation of ownership from control. Separate body to outline the organization, purpose value and structure and members that implement roles and values defined by governing bodies. Here members are the managers who act day to day functions and governing bodies who act as actively looking a mistake made because of failure to notice or ensure in right direction. Management is routine administrative work related to daily operation of business. While doing business transactions investors (shareholders) expect from board and managers what they should and should not do with their power over corporations. They also have right to receive certain part of profit from their investment made. Shareholder maximization of wealth is main concern of members with successful operation of corporation. Board should not decide or act in a way that would harm the corporation objective and purpose and managers should not steal from the company they work. They should avoid such transactions that place them in conflict of interest between the obligation to corporations and their personal financial objectives.

Corporate governance arises so as to reduce the conflict of interest of the corporations or say to reduce the agency cost between shareholders, board and managers. That influences the running of corporations effectively. Anything and everything that influences the way the corporation run falls within the definition of corporate governance. Say the exercise of decision making power in the corporation is corporate governance.

In general, corporate governance is a part of company law. Economic law is wider that includes company law. Economic law encompasses the certain subjects like competition law, Intellectual property law, financial law, WTO and Company law. We might have some queries in our mind about company law- it is all about that applies to rights, relations and conduct of persons, companies and business organisations. Corporate law is broader companies' law. But what about corporate governance, does it matter to law? What are legislative, regulatory and other corporate governance sources? What are current issues, development, trends and challenges in corporate governance? Is corporate governance guided by certain principles, if yes, then what are those principles and who are the active players in corporate governance?

The Cadbury report on corporate governance in 1992 UK recognize is the relation between the economy and company law stating a country's economy depends upon the drive and efficiency of its companies because company law regulated business entities like private company, single holder company, public companies. As we know that public companies share is transferable. Companies or corporation are exchangeable used but corporate governance is used mostly in corporations that are listed companies the large scale business companies need to be listed in recognized stock exchange in doing the buying and selling of securities. Corporate law is where corporate governance is abundantly present. At first governance refers to process by which decision related to risk management and compliance are made within an organization. The main aim of corporate law is to regulate corporate form. Regulation in field of corporate governance is important aspect of corporate law of its governance have wide and no uniform definitions. The word corporate governance was used by the Cadbury report of UK in 1992 States corporate governance is a system where companies are directed and controlled. Dutch corporate governance report identifies as integrity, transparency, proper supervision and accountability. Many people have doubt that is corporate governance a part of legal concept or not? To answer this, it is a process, customs, policies and laws by which corporation is directed, administered and controlled, this term describes the right and responsibilities are shared between the various corporate participants especially management, board and shareholders.

In the view of Jesesn, Meckling Winter, Easterbook and Fischel corporation as an all ' nexus of contracts' among constituencies including managers, shareholders, creditors, employee and others. Corporate law and governance mainly focus on agency relationship between managers and shareholders. The law of corporate governance establishes "rules of game" among the corporate constituencies. OECD Principles of Corporate Governance states:" Corporate

governance involves a set of relationships between a company's management, its board, its shareholders and other stakeholders. Corporate governance also provides the structure through which the objectives of the company are set, and the means of attaining those objectives and monitoring performance are determined."

The main Theory on agency problems conflict between shareholder and non-shareholders, it is important to understand who's who in corporate governance. It is first the matter of manager and owners. Directors- include insider or outside(independent), shareholders(individuals, pension plans, hedge funds, mutual Fund, institutional investors) and stakeholders- employee, creditors, customer, suppliers, communities) having interest in the activities and management of the companies.

Generally corporate governance focus on relationship between corporate managers, board of directors and its shareholders. In wide sense, definition includes relationship of corporations to all its stakeholders and society and covers set of laws, regulations, listing rules that attract capital, perform efficiently, generate profit and meet both legal application and general societal expectations.

Corporate governance is answered differently in different part of the world, in Europe and Asia based on stakeholder centric model argues manager and boards are expected to concern themselves with interest of employee and other stakeholders such as suppliers, creditors, tax authorities and communities in which they operate. In Anglo-American approach(UK, USA, India) emphasis primarily of ownership and property rights and its primary focus on creating shareholder value.

At present we have seen that companies operate business structure has become more complex. Most especially for the listed companies who make their business in large capital, they make initial public offering, further public offering and issue of bonus shares, etc. To raise capital in business operation. They have large number of investors, investors investment must have confidence in investing in such companies having good corporate governance good corporate governance is widely accepted as global business standard. The collapse of big corporations after 1980's and crisis in Asia increased the height debate on corporate governance. The causes of corporate failure were found due to lack of inadequate regulatory mechanism including unethical business conduct, failure of boards of directors, lack of information flow among the management, fraud in audits, weak internal control, unaccountability, responsibility of boards, are the common problems in corporate governance. Corporate governance as regulating the corporations socially, economically and environmentally responsible in order to protect the interest of stakeholders or reduce the loss

or adverse impact as a result of operational activities or decision of hierarchy management.

There are some guided principles for companies by regulatory body to comply with law, securities law and listing requirements which is an instrument that governs the transparency, accountability, responsibilities of directors, shareholders, integrity and social responsibility in decision making process of business. They are applied to basic overview of any corporation with basic norms, duties and disclosures.

Corporate governance is related with a different multiple issues in a field of corporate law, securities regulations, corporate finance, industrial Relations. According to Cioffi's definition it is a Nexus of Institutions define by company law, financial market regulations and labour law.

Corporate Law generally tries to reduce the cost of entering a business that means reduce the role of single person or few people and dealing of business. Where the risk is reduced with several of parties like shareholders, entrepreneurs (board that makes vision mission and strategy to achieve a business object) and managers say executive who carry out day to day operation of company. Good corporate governance helps to increase share price and makes it easier to obtain capital. Investors are hesitant to lend money or buy shares in a corporation that does not subscribe to good corporate governance principles. Transparency, independent directors, and a separate audit committee are especially important. Some international investors will not seriously consider investing in a company that does not have these things.

The detail study of corporate governance and its principles are matter of state regulation, governance codes, securities law and company law. Countries have different codes of governance determined by the political, economic, legal and cultural aspects of state. The adoption of principles of corporate governance is important to ensure that if mechanism is adopted that would lead to the solving the governance problems. The major issue is controlling the majority shareholder and protection of minority shareholders. For example, Russian code has given strong emphasis in protection of minority shareholder, and India's legal system having best investors protection in the world. It is important for enterprises to be governed by more investor-friendly laws or directing their portfolio companies to shareholder-friendly domiciles, competition for capital could turn the race to the bottom into a race to the top.