

AN EMPIRICAL STUDY ON CORPORATE GOVERNANCE IN SMEs

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ABSTRACT

SMEs play a very crucial role in the development of the economy and also help in poverty reduction. It also helps in boosting the rate of GDP and increases the standard of living of people. Corporate governance is now seen as an essential building block of stable economies. It helps to protect the rights and interests of shareholders and, increasingly, those of other stakeholders, providing a framework for effective monitoring of management actions and performance and for encouraging better business results. This paper discusses how implementation of corporate governance develops the SMEs as well as economy. In this paper, 10 parameters are taken into considerations to study the corporate governance of SMEs for two years i.e., 2012-2013 and 2016-2017. The research paper has been prepared with the help of secondary data only and the list of SMEs listed in BSE is evaluated with the help of their annual reports. The study was aimed to analyses the corporate governance in these SMEs.

KEYWORDS: *Corporate Governance, SME, Stakeholders, Financial Disclosures and Performance*

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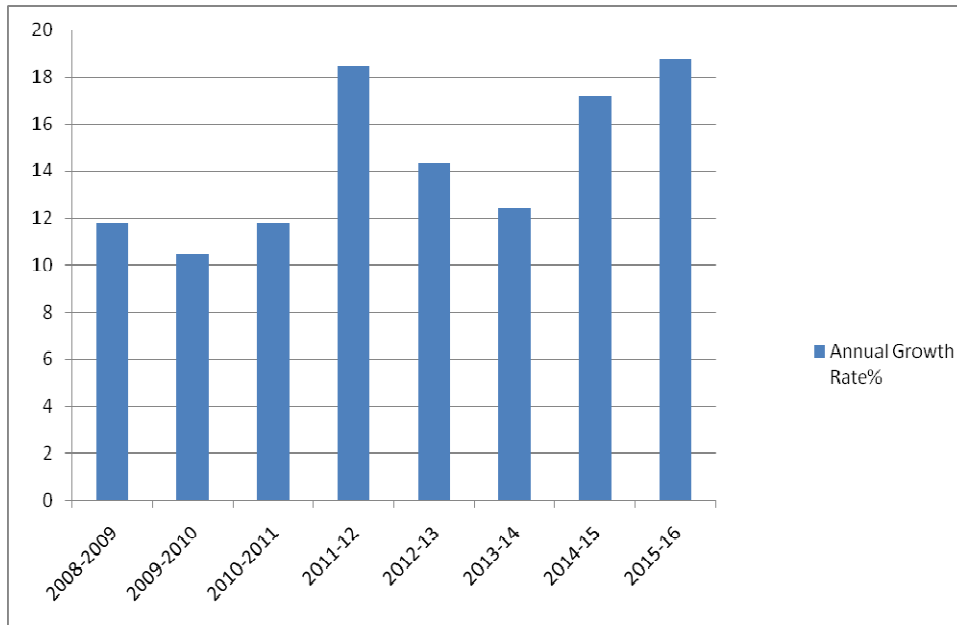
INTRODUCTION

Conceptual Framework

Corporate Governance has become a phenomenon that attracts a lot of interest in business. Corporate Governance is basically the relationship between shareholders and management board within an institutional framework. There is a strong link between corporate governance and economic development. Good corporate governance leads to high profit which contributes in the GDP of the country. Corporate governance is the effective tool to lead the corporate market. Effective corporate governance leads to effective growth of the economy and also provides employment opportunity. The quality of corporate governance is linked to the framework. The government plays a central role in developing the framework under which policies are developed.

Small Medium Enterprises are the backbone of the Indian economy and promotes the balanced economic development. SME sector has rapidly grown over years and contributes almost 40 percent of the total industrial output. They contribute to economic development by creating employment for both rural and urban population. Small Medium Enterprises create an opportunity in income generation for people and a critical vehicle for poverty reduction in India. This concept has introduced to protect the rights of shareholders in the organization. SMEs are the engine of growth in the economy as they contribute to employment and poverty reduction. In the developed economies, SMEs are the main contributors of GDP. SME sector will provide sustainable growth and generate jobs.

The primary objectives of the study is to analyse the impact of reforms of corporate governance in SMEs and to study the implementation of corporate governance in Indian corporate. Also a score has been developed to study the corporate governance practices in 40 SME sector companies.



Source: Annual Report, MSME, 2015–16

Figure 1: Annual Growth Rate %.

LITERATURE REVIEW

The corporate governance concept emerged in India after the second half of 1996 due to economic liberalization. With the changing times, there was also need for greater accountability of companies to their shareholders and customers.

Mehta G.S (2003) in his article titled with ‘Dharma in Corporate Governance’ explains the meaning. The definition explains how important it is to follow corporate governance in the era of globalization. At the end he remarked that a policy towards consistent and transparent corporate behavior should be adopted including public justification of major strategic decisions. Dharma, Jigyasa are the core values of the rich Indian philosophical tradition and these are the guiding forces towards the corporate governance. Shahnawaz Mahmood (2008) article highlights that corporate governance is not only important for large companies but also small and medium enterprises. SMEs around the world are increasingly becoming aware of the importance of good, trusting relationship with customers, employees, suppliers and government. Cochran and Warwick (1988) define corporate governance as an umbrella term that includes specific issues arising from interaction among senior management, shareholders and other corporate stakeholders. Schrieffer and Vishney (1997) define as the ways in which suppliers of finance to corporations assure themselves of getting a return on their investments.

Data Collection and Analysis

Data Collection

The data for the study is collected through secondary data by means of the annual report. 10 parameters of corporate governance have been taken into consideration. The sample size of data is 40 BSE listed SMEs. The parameters of all 40 SMEs are given score according to which the data is analyzed. Each parameter score can be given 1, 2 or 3. Then, the

percent is calculated of every parameter. The data is taken for 2012-13 to 2016-17. The percentage of all 10 parameters is calculated for both the respective years.

Table 1

Parameters		Score
No. of board of directors	Upto 6	1
	6-10	2
	> 10	3
No. of independent Directors	1/3	1
	1/3-1/2	2
	> 1/2	3

The score is also given to all SMEs and the percentage of corporate governance followed in 40 SMEs are also calculated.

Table 2

SMEs	2012-13 Score	Percentage	2016-17 Score	Percentage
Ambika Cotton Mills Ltd.	14	63.63	7	31.8
Anisha Impex Ltd.	14	63.63	15	68.18

Data Analysis the technique of hypothesis is 2 tailed t-Test which is applied after giving score to parameters of Corporate Governance.

Data Analysis

All the parameters are given score and then percentage is calculated by dividing it by total score.

Board of Directors

The board of directors should constitute combination of both executive and non executive directors. The percentage of board of directors is increased but then SMEs should increase the no. of board of directors too, as it is not so good. It will help in increase in efficiency.

Table 3

Parameter	2012-13 Score	Percentage	2016-17 Score	Percentage
No. of Board of Directors	65	54.16	66	55

Number of Independent Directors

According to the clause 49, independent director is defined as any person who is non executive director who passes his knowledge to the company. The independent directors if wants can hold a meeting in which no other member is allowed. The percentage of number of independent directors are decreasing to 69%.

Table 4

Parameter	2012-13 Score	Percentage	2016-17 Score	Percentage
No. of Independent Directors	91	75	83	69

No. of Meetings of the Board of Directors

The first board meeting should be held within 30 days of incorporation. In case the board meeting is called at shorter notice then it is compulsory that at least one independent director should be present in the meeting. SMEs should increase their no. of meetings as the percentage is falling.

Table 5

Parameter	2012-13 Score	Percentage	2016-17	Percentage
No. of meetings	87	72.5	83	69.16

Average No. of Meetings Attended By the Board of Directors

There is an increase in the average no. of meetings attended by directors from 68% to 74%. But then the board of directors should attend more meetings.

Table 6

Parameter	2012-13 Score	Percentage	2016-17 Score	Percentage
Average no. of meetings held	82	68.33	89	74.16

No. of Committee

The company should have more and more committees as more score is given to those SMEs in which there are more no of committee. According to the rule, audit committee must meet 4 times in a year. The committees investigate in an activity, seek information from employee. The no. of committees are increasing but SMEs should increase more committee.

Table 7

Parameters	2012-13	Percentage	2016-17	Percentage
No. of Committee	51	42.5	62	51.66

No. of Committee Headed by Independent Director

There is an increase in no. of committee headed by independent director but not satisfactory. SMEs should increase the committee headed by independent director.

Table 8

Parameter	2012-13 Score	Percentage	2016-17 Score	Percentage
No. of Committee Headed by Independent director	44	36.66	47	39.16

Separate Meeting of Independent Director

Independent directors must hold at least 1 meeting in a year in which others members and non independent directors are not allowed. The independent directors can view the performance of chairperson and other members in the company. Separate meetings of independent directors increased 3 times from 2012-13 to 2016-17.

Table 9

Parameters	2012-13 Score	Percentage	2016-17 Score	Percentage
Separate Meetings of Independent Directors	4	10	12	30

No. of Women Directors

It is compulsory for all the listed companies to appoint at least 1 woman director as per corporate governance norms. There is an increase in percentage of women as board of director which would have a positive effect. But then also SMEs should increase more number of women directors.

Table 10

Parameter	2012–13 Score	Percentage	2016–17 score	Percentage
No. of women director	21	52.5	25	62.5

Whistle Blower Policy

According to the clause 49, it is compulsory to establish a system to directors and employees to report about certain unethical behavior, fraud. It should provide the safeguard against the person who report any concern. There is an incredible increase in percentage of SMEs following this policy.

Table 11

Parameter	2012–13 Score	Percentage	2016–17 Score	Percentage
Whistle Blower Policy	13	32.5	25	62.5

Code of Conduct

According to the clause 49, it is compulsory for the board of directors to lay down the code of conduct for all the members as well as senior management. Independent directors will be held responsible for the acts of omission which had occurred. It is good that almost all the companies are following code of conduct and are scored very better.

Table 12

Parameter	2012-13 Score	%	2016-17 Score	%
Code of conduct	39	97.5	38	95

Data Analysis

Table 13

Paired Samples Test			
		Difference	Sig. (2-tailed)
No. of board of Directors	2012–2016	39	.534
No. of independent directors	2012–2016	39	.160
No. of meetings	2012–2016	39	.440
Avg. no. of meetings attended	2012–2016	39	.164
No. of committee	2012–2016	39	.001
No. of committee headed by independent director	2012–2016	39	.183
Separate meeting of independent director	2012–2016	39	.019
No. of women director	2012–2016	39	.160
Whistle Blower Policy	2012–2016	39	.002
Code of Conduct	2012–2016	39	.323

From the above research it is clear that most of the SMEs are growing but still the percentage is not satisfactory. Out of 10 parameters which are taken into consideration some of the parameters are being followed in SMEs but not all. Parameters which are shown in yellow are common parameters than others. Parameters which are in blue are less aware than yellow one. Mostly common parameters are Number of committee, separate meeting of independent director and whistle blower policy.

Findings

In recent years, the concept of corporate governance has emerged significantly. Many SMEs listed in BSE has adopted the concept of corporate governance. Research shows that corporate governance is linked to their company's profit and efficiency. Good image is created if corporate governance is followed. Total score is given to each company and then

percentage is calculated from which comparison can be done. Not all the companies emerged with this concept but more than half of companies grew with this concept. In recent years, the concept of corporate governance has emerged significantly. Many SMEs listed in BSE has adopted the concept of corporate governance. Number of committee, separate meeting of independent directors and whistle blower policy are the parameters which are mostly followed by SME's. No. of independent directors, average no. of meetings attended by directors and no. of women directors are the parameters which are less followed than above ones. Ambika Cotton Mills Ltd. is the SME which least follow Corporate Governance i.e., 31.8% and Kirloskar Oil Engines Ltd. follows the most i.e. 90.9%.

CONCLUSIONS

From the research it is clear that it is important for SMEs to adopt the concept of corporate governance. In recent years, almost every company is following it and becoming aware of it. This help in increasing the efficiency in the company and create more potential image which as there is transparency, accountability which help SMEs to access finance. It is evident from above that it is necessary to adopt better corporate governance norms with ethical code of conduct business framed by government. Implementation of corporate governance helps in achieving confidence among shareholders and gain trust through the company. This will ultimately help the company to achieve their target.

Better corporate governance leads to more profitability and better image. The aim of corporate governance is to protect the rights of the shareholders and maintain the standards of disclosure and transparency. It maintains the standards for ethical code of conduct and behavior for day- to – day activities. From the research it was found that more half of listed SMEs follow corporate governance and is increasing day by day. This concept is gaining more and more importance as there are many norms which have been set up by government. So, it becomes compulsory to adopt these norms by the SMEs.

RECOMMENDATIONS

- Corporate Governance should be incorporated in Companies Act, 2013 so that every SME would follow which will result in more profitability of SME in the long run.
- Good corporate Governance would enable the SME to grow faster.
- The SMEs should increase the number of directors as it increases efficiency.
- As the number of independent directors are not satisfactory, therefore, SMEs should increase the number of independent directors.
- The percent of separate meeting of independent directors is quite low therefore SMEs need to conduct more meetings.
- Despite of provision of compulsory appointment of women director in all listed companies, the percentage is quite low. Therefore, SMEs should increase the proportion of women director.
- SMEs should follow whistle blower policy to increase more transparency.

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She is currently pursuing M.com from Amity University (AU), Noida, Uttar Pradesh. She has interest in area of Finance, Business Ethics, Corporate Governance, Accounting, Banking and many more. She has presented the research paper in International Conference which is conducted in Amity University and has been collaborated with Kingston University, London. She has also attended many conferences and seminars. She had qualified graduation with first division. She has interest in area of research and would be pursuing her Doctor of Philosophy in future.