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DYNAMICS OF CORPORATE GOVERNANCE IN PRACTICE



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Abstract: In this connection it is interesting to observe the findings which the American Management Association published in 1952 giving the result of survey of one hundred large corporations (over 5,000 employees) the purpose of which was to ascertain the number of executives reporting to the president. The findings clearly show the extent and nature of the span of management as it is actually found in industry. The number of executives reporting to the president is clearly larger than the number advocated by several writers on this subject. "Though prevailing practice does not necessarily prove the correctness of policy, the action of successful company presidents, often under competitive conditions should be taken into account." Generally the number of executives reporting to the president range from one to twenty four, with the median number of subordinates supervised by the president between eight and nine. In a similar survey covering forty one medium sized corporation (500 to 5000 employees), the median was found to be somewhat lower than in larger companies, with between six and seven subordinates reporting to the president. The range between the lowest and highest number of executives reporting is also less. Date feels that "the reduced median and range reflect the lesser volume of important problems faced by the smaller corporations and smaller number of people required to assist the president in coordination and control."

Key words: Dynamics, management, terminology.

INTRODUCTION:

In order to assess these findings properly, as the A.M.A. survey clearly points out it is important to note that interpretation of the term "reporting to" made by different corporations range all the way from occasional "access to" the superior to direct and constant supervision. The findings seem to indicate that the number of subordinates having access to an executive is much larger than the number of subordinates under his close and intensive supervision. The concept of "access to" an executive is one of into the production, sales, and finance departments. These are the three major functions which will be found in almost all business corporations and without which the corporation could not exist.

The terminology is not always the same due to different character of the undertaking. The nature of the business might be such that the production function will be replaced with "buying" as is the case in the activities of a distributorship. In the functions of an airline company, production is called "operations," whereas for sales the term "traffic" is used. A railroad divides its functions into what it terms operations, traffic, and finance. All of this is primarily a difference in terminology. In the operation of hospital one hardly finds a distinct selling function, but this does not mean that this activity is not undertaken. It merely indicates that in such an enterprise selling plays a minor role as a result of the nature of the enterprise. In such an instance it does not need any emphasis as a special enterprise function. For all practice purposes, however, we will find a great many

enterprises which are departmentalized according to their major functions: production, sales and finance. This does not mean that functional departmentation is used exclusively; it can be found employed together with the other guides of departmentation, such as product, territorial, or customer departmentation. But somewhere in the organization, almost every enterprise has some functional departmentation with its organizational setup.

Almost every enterprise begins its existence with a functional organization structure. It is the best type of organization structure for a younger, small business created by one or a few people. Such a new enterprise is normally small, and all the work is closely supervised by the proprietor. The immediate problem is to get things done, and emphasis is more on operations than on management. It is probable that at a later time, after the enterprise has grown into a large corporation, the question will arise concerning at what point the corporation should change from functional departmentation to a different type of departmentation. But in its inception the functional type of structure is the most logical.

Departmentation by enterprise function means to group all the work to be done into major functional departments. All work of the same kind and all manufacturing in charge of all manufacturing activities throughout the enterprise, regardless of where the plant might be located and regardless of how many products lines are being manufactured. For example, in a corporation which has been organized for the purpose of manufactured wooden

and metal furniture functional type departmentation will be as shown in figure 1.

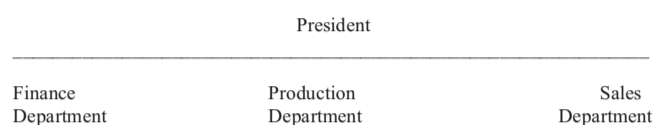
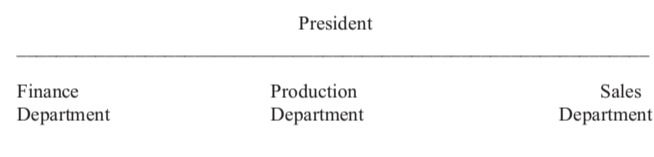


Figure 1

In this corporation both wooden and metal furniture products are manufactured in the sample plant, and both types of furniture are sold by the same sales people. As this enterprise grows and undertaken additional work, these additions are made to already existing function. If, in our example, the corporation should decide to add plastic furniture to its product line, the add duties in the manufacturing and sales functions are made within the existing functional structure. Such increased activities will of necessity mean adding levels of supervision to the managers within the functional departments as shown in figure 2.

In most enterprises production, sales and finance are undisputedly the major functional departments, and the managers of these are from the primary level and report directly to the chief executive, usually the president. Under the departments are found those which have large budgets, which employ many people, and which are essential to the existence of the form and essential to reaching the objective of the enterprise.



Sometimes a major function become a minor function a certain time, for instance, the function of the sales department during war periods. Up until wartimes, selling is one of the major functions of the enterprise. During war, however, with the advent of shortages selling is no longer a problem. The problem, rather, is the one of allocating the available finished product to the many orders. Hence, possible even a minor function of sales has become less important. This changes, however, once hostilities end; selling again becomes one of the major functions with the return of a buyer's market. Such a change could also work in the reverse. In a certain enterprise, for instance, research work had been only a minor function, but as time went on research in this firm became the lifeblood of the enterprise; hence it is now considered a major function.

ADVANTAGES OF FUNCTIONAL DEPARTMENTATION

There are many advantages to functional departmentation. First, it is a natural, logical way of arranging the various activities of the enterprise. The functional type of structure facilitates and makes use of the advantages of specialization leading to economic operation.

It facilitates coordination and makes the skills and abilities of one or few top people in the primary activities available to the entire enterprise.

Functional departmentation take advantage of occupational specialization by grouping together the functions which belong together and which are performed by the same specialists with the same kind of equipment and facilities. Each manager is concerned with one type of work only, and all of his energies will be concentrated on it. This leads to economic operations as it will make maximum use of the available equipment and facilities. If all production is concentrated in one department, peak and valleys in the demand for one product can probably be minimized by valleys and peaks of another product. Additional economies are produced by pooling and combining, receiving, shipping, maintenance and a number of other administrative expences.

Functional departmentation also facilitates coordination within the function since one manager is in charge of all of one type of activity. It is simpler to achieve coordination with one function than it would be in an organization where the same function is performed in several different divisions. Another advantage of functional departmentation is that it makes the outstanding abilities of one or a few individuals available to the enterprise as a whole. "The reason for this is that, in the functional organization structure, only the president is so placed organizationally, as to be able to coordinate problems and make decisions having to do with one or more of the major functions. As a result, the structure itself forces all such decisions to the top and ensures that the special abilities of the chief executive can be transmitted to the point of action in most of the important affairs of the company." It is proven method which can easily be justified by management. It is a method which has been successful over the years and it is a simple method. In short, it makes good sense.

DISADVANTAGES OF FUNCTIONAL DEPARTMENTATION

Although the above is an impressive list of advantages of functional departmentation, they eventually turn into disadvantages as the enterprise grows in size and diversity. With the growth of the company, centralization will become excessive, leading to increasing delay in decision making. It also will become increasingly difficult to exercise control and measure performance, and a possible shortage in managerial talent will result. As the company grows there will be a larger total number of people reporting to supervisors. This will show down communication. Because of the nature of the organization structure, coordinating decisions that affect two or more different functions can only be made at the top of the organization namely be chief executive. This is the only point at which sufficient authority and information are available to make such a decision. This, of necessity, leads to delay in decision making and leads to a long road for decisions to filter from the top to bottom of the pyramid.

Functional departmentation makes effective control difficult. The manufacturing departments produces all products and it is difficult, if not impossible to single out

the cost of any one product. For a long time such functional departmentation prevented the Chrysler Corporation from determining accurately the cost of producing a Plymouth or any of the other cars. In contrast, automobile manufacturers who do not have functional departmentation and who operate on a product divisions basis can readily establish the cost of each of their particular makes.

Another disadvantage of functional departmentation is that it does not offer a good training ground for all round managers. A Manager in such a functional structure has little opportunity to learn to manage the entire range of the different functions. He will become an expert in only one particular function and tend to de-emphasize the importance of the other functions. Once he is transferred from a managerial position in one particular function to a top managerial job, there is the danger that he will continue to carry with him emphasis on the function from which he originally came. It happens often that a former sales executive who becomes the president of a company is still primarily concerned with sales instead of devoting all of his energies to the overall managerial functions of the enterprise. This, of course is not a shortcoming of departmentation; it is the fault of the executive. However, departmentation by functions can easily lead to this particular kind of managerial preoccupation.

Time for Change

Although functional departmentation is the most logical one to choose in the early stages of the enterprise, sooner or later the manager must decide at which point he should change the corporation organization from functional departmentation to any of the other types of organization. There is no single answer as to the point of which such a change is advisable, and it takes a thorough analysis of the organization before such a decision can be made. It would be wrong to decide such a question based merely on the amount of sales transacted by the enterprise. In the case of a firm doing less than ten million dollars sales a year, for example, it might be better to departmentalize it on another basis rather than on the basis of the functions. It might be more advisable for such a corporation to departmentalize by products or by territories. On the other hand, it is interesting to note that in 1920 when General Motors switched from a functional structure to product divisions the total volume was in excess of five hundred million dollars annual sales. In each case it takes a thorough analysis to decide whether the enterprise has outgrown the original functional departmentation which has brought about the initial success of the corporation and brought it to the point where it stands now.

Departmentation by Product

When the size of the enterprise has grown such that all the original advantages of functional departmentation have turned into disadvantages and the organization has developed to be a large and monolithic one, management will decide that it is necessary to change from the functional structure of the organization to a different one and will seriously consider departmentalizing by products in a product line as a relatively autonomous, integrated unit within the overall framework of the corporation. Emphasis is

shifted from the function to the product to be manufactured and sold.

Under this product departmentation an executive will be in charge of and responsible for all the activities relating to particular product. He will have extensive authority over the manufacturer, sales, service and engineering functions which pertain to this particular product. He will have extensive authority over the manufacture, sales, service and engineering functions which pertain to this particular product line. In order to make a product division successful, it is necessary to place within this product division all the activities which are needed to perform effectively the operations. In product departmentation it is of no importance where the divisions is located, whether it is close to the home office or geographically far removed. It is the product around which the divisions is organized and not a territory.

The adoption of product departmentation will divide the large corporation into smaller units will recapture some of the advantages of a smaller functional organization. As mentioned in the discussion on functional departmentation, most disadvantages appeared when the functional organization had grown to a large size. Product departmentation permits a division into smaller administrative units. By putting emphasis on product departmentation, expansion, improvement, and diversification of the product will be encouraged. The manufacture, marketing, and engineering of this particular product will be of primary concern to the manager of this division. There is no doubt that in a functional organization where several different products are manufactured and sold by the same organization, some of these products will receive more emphasis than others. Although such emphasis is perfectly normal and understandable, it may be harmful to some of the products, particularly products which require more promotion and more sales efforts in order to achieve their place in the market. Problems of this sort can be taken care of by product departmentation, something called product division. In the case of the enterprise which manufacture metal wood, and plastic furniture and decide to departmentalize on a product basis, the organization would appear as indicated in figure 3. In this example, each product is co-ordinated at the top of the product grouping, namely, at the divisional level. The president will retain his own centralized advisory groups which help him in the overall management of the enterprise. Product departmentation has proved successful in all functional areas with the exception of such activities as industrial relations and finance. It is essential that labour relations should remain centralized particularly when dealing with a large national union. For obvious reasons, it is also desirable that overall financial management should be largely retained by the president of the enterprise and top management. It matters little whether the different plants are located close to the home office or are remote.

The decision whether or not to departmentalize by products will largely depend on whether or not the characteristics of the manufacturing, engineering, and selling of the particular products lend themselves to such product departmentation. Each product should be suitable

for separation from other products, and having its own production families and sales organization should bring about the best results. The best known examples of product departmentation or product division are the various divisions of General Motors- Buick, Cadillac, and the others. The Du Pont Corporation is another excellent example of an enterprise which, around 1921, decided that product expansion departmentation, grouping its departments along principal product lines. Within each department, production, sales, and research are established as a line division. The manager of each of these three functions reports on the same level directly to the general manager of the individual product division.

There are several other leading companies that are organized along the lines of different products or merchandise lines for each department. One also finds the same product departmentation, so to speak, in commercial banks which within the loan activities have, for example, separate loan departments for commercial, personal, and industrial uses.

This grouping of departments can at times lead to difficulties in coordination within the organization structure. It can happen that successful manager of a product division will try to acquire more and more power and to enlarge his empire. Danger from this direction can be guarded against by the existence of a general staff, by centralization of finances, and by major policy determination by the top management of the enterprise. This, broadly speaking is the arrangement at General Motors Corporation, Du Pont, and other enterprises; decentralized product division with centralized control at headquarters.

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