Corporate Governance: Literature Review on Agency Costs and Pieces of Evidence on Different Perspectives

Shubhi Agarwal and Archna Singh***

This paper intends to review different pieces of literature that try to establish a link between the tools of corporate governance and agency costs. Tools of corporate governance play a key role in reducing agency costs. The paper focuses on reviewing the literature on ownership structure, firm structure, board structure, and remuneration structure extensively. The paper reviews many aspects of ownership structure as well as firm structure, i.e., institutional ownership, non-institutional ownership, managerial ownership, firm age, and firm size. The works of literature have cited many way outs as strong institutional ownership, managerial ownership, board size, frequency of board meetings, board independence, board composition, board ownership, remuneration structure, and firm age as well as size can be beneficial in eliminating agency costs. The paper uses a descriptive research design. A lottery system of random sampling is used while selecting different kinds of literature reviews of ownership as well as remuneration structure. The paper takes the 2004-2019 time period for reviewing literature. The period is selected based on convenience sampling. The extensive review of literature will enlighten the research scholars as well as academicians in understanding the problem of agency and how tools of corporate governance will help in reducing agency costs.

Introduction

Agency model starts from the conflicts which arise between principal and agents who are functioning in corporate firms. The agency problem was an ancient phenomenon when human civilization did businesses and wanted to maximize their profits. Agency issue is one of the age-old issues that have persisted since the development of the joint-stock companies. Every corporate firm suffered from the agency problem, so it is essential to provide light on this concept at the present juncture. Over time, the agency problem has been seen in various ways and the many pieces of literature have provided valid evidence for it. The discussion on the literature of agency costs and many tools of corporate governance is essential to understand and explore agency problems. It is essential to focus on specific tools of corporate governance that helps in mitigating agency costs. The relevance of the agency problem has been vastly

* Ph.D. Scholar, Department of Economics, Meerut College, Chaudhary Charan Singh University, Meerut, Uttar Pradesh, India; and is the corresponding author. E-mail: shubhiagarwal1001@gmail.com

** Associate Professor, Department of Economics, Meerut College, Chaudhary Charan Singh University, Meerut, Uttar Pradesh, India. E-mail: drarchnasingh@yahoo.com

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witnessed in different academic groups and categories. The verification and affirmation are showed in many fields like economics (Spence and Zeckhauser, 1971; Ross, 1973; and Jensen and Meckling, 1976); accounting (Watts and Zimmerman, 1983; and Ronen and Balachandran, 1995); organizational behavior (Kosnik and Bittenhausen, 1992); finance (Fama, 1980; Fama and Jensen, 1983; and Jensen, 1986); marketing (Bergen *et al*., 1992; Logan, 2000; and Tate *et al*., 2010); sociology (Kiser and Tong, 1992; and Adams, 1996); and political science (Weingast and Moran, 1983; and Hammond and Knott, 1996). The vast presence of the agency problem in different types of corporate firms has made this model one of the most essential models in the finance and economic literature.

The main aspect of this paper is to inspect and analyze extensive empirical literature on agency costs to understand the appropriate answers to certain essential questions. These questions are as follows:

How will institutional ownership, foreign ownership, insider ownership, and managerial ownership help to increase corporate financial performance and reduce agency costs?

How will firm age and firm size contribute to mitigating agency problems and enhance corporate performance?

And how will remuneration structure (executive compensation, director's remuneration, and director's fees) bring a reduction in agency costs?

These issues have dominated the finance literature for the past many decades. This paper is developed in the same line with extensive work on the empirical literature on the various aspects of the agency costs. This paper chooses the empirical evidence of ownership, firm, and remuneration structure in the popular areas of agency costs.

Objective

To review the different as well as extensive pieces of literature depicting the link between ownership, firm, board as well as remuneration structure and corporate firm performance which ultimately contribute to mitigating agency costs.

Data and Methodology

The main aim of this study is to explore the empirical works done on agency costs and different tools of corporate governance. This review of literature will help in finding solutions to the major problem of agency costs which are faced by almost every corporate firm irrespective of whichever field it belongs to. The design of this literature review is based on one basic approach that deals with empirical studies conducted focusing on reducing agency costs.

Research Design: The research study has a descriptive research design.

Sample Design: The lottery method of random sampling is used while selecting different pieces of literature review of ownership, firm, board, and remuneration structure.

Target Population: The target population is to consider research studies conducted on establishing the link between corporate governance mechanisms and agency costs worldwide.

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Study Period: This research study took the 2004-2019 time period for reviewing the literature. The period is selected based on convenience sampling.

Data Collection Method: This study uses secondary data. The authors have explored many journals, books, and chapters available in online databases like JSTOR, Springer, SAGE, National Digital Library, etc.

Agency Costs and Ownership Structure

Agency theory furnishes that ownership structure plays a key role in mitigating agency costs. Some research studies Zeckhauser and Pound (1990) and Shlefier and Vishny (1997) stressed that concentrated ownership can monitor the managerial employees' working style closely to mitigate agency costs. Table 1 depicts the empirical research studies conducted by eminent academicians and scholars and their result findings. The research studies mentioned have used institutional ownership, foreign institutional ownership, state/government ownership and block holder ownership as the ownership structure variables.

Table 1: Impact of Ownership Structure on Corporate Performance and Agency Costs

Author	Year	Country	Sample	Findings
Bhattacharya and Rao	2005	India	Sample of 76 companies from 2001 to 2003	The negative impact of foreign institutional investors on agency costs. The direct impact of board size on agency costs.
Zuobao *et al.*	2005	China	Sample of 5,284 firms from 1991 to 2001	The negative impact of state ownership and institutional ownership on the market valuation and the significant positive impact of foreign ownership on market valuation and helps in reducing agency costs.
Uhomoibhi	2007	Nigeria	Sample of 98 banks from 1989 to 2004	Insignificant impact of ownership structure on the profitability of Nigerian banks and agency costs.
Xiao and Yuan	2007	China	Sample of 559 companies of 2002	The direct impact of block-holder ownership and foreign ownership on the voluntary disclosure and hence reducing agency costs.
Ajina and Lakhal	2010	Indonesia	Sample of many firms from 2002 to 2007	The direct impact of institutional ownership on the liquidity of the corporate firm.
Charfeddine and Elmarzougui	2010	France	Sample of 35 firms from 2002 to 2005	The positive impact of institutional shareholding on

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Table 1 (Cont.)

Author	Year	Country	Sample	Findings
				the firm financial performance and thereby reducing agency costs.
Liang *et al.*	2011	Taiwan (Republic of China)	Sample of 4,443 corporate firms from 1999 to 2008	The positive influence of ownership structure on corporate performance and helps in mitigating agency costs.
Fazlzadeh *et al.*	2011	Iran	Sample of 137 corporate firms from 2001 to 2006	Inverse impact of concentrated institutional ownership on firm performance.
Anthony and Chinaemerem	2012	Kenya	Sample of 62 firms from 2009 to 2013.	The direct impact of concentration ownership on the firm financial performance and helps in reducing agency costs.
Ibrahim	2012	Ghana	Sample (Cal Bank, HFC, Ecobank Ghana Limited, Ghana Commercial Bank, SG-SSB, Standard Chartered Bank) of financial firms from 2005 to 2009	The significant but negative impact of ownership concentration on firm financial performance but the direct impact of insider and institutional ownership on firm financial performance.
Fauzi and Locke	2012	New Zealand	Sample of 79 corporate firms	Inverse impact of institutional ownership on the firm performance and does not help in mitigating agency cost.
Juhmani	2013	Bahrain	Sample of 50 corporate firms	The negative impact of block-holder ownership on the voluntary disclosures and insignificant impact of managerial ownership and governmental ownership on the voluntary disclosures.
Miguny *et al.*	2013	Iran	Sample of 111 corporate firms from 2006 to 2011	Inverse impact of institutional ownership on the net earnings and hence, agency cost of corporate firms.
Sivathasan and Sangeetha	2013	Sri Lanka	Sample of 287 firms from 2009 to 2011	The direct impact of foreign ownership on leverage but the negative impact of

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Table 1 (Cont.)

Author	Year	Country	Sample	Findings
				domestic ownership on the leverage.
Benjamin *et al.*	2014	Nigeria	Sample of 17 firms from 2001 to 2010	A direct and significant impact of ownership structure on the firm performance and helps in eliminating agency costs.
Yegon *et al.*	2014	Kenya	Sample of nine corporate firms from 2008 to 2012	Institutional ownership makes an effect on agency costs while external ownership does not make an effect.
Shahid	2014	Pakistan	Sample of 80 firms used from 2005 to 2009.	The negative impact of insider ownership on return on assets but the positive impact of independent directors on market performances indicators.
Alexander *et al.*	2014	Ghana	Sample of all firms listed in Ghana Stock Exchange from 2008 to 2012	The negative impact of concentrated ownership on firm performance but managerial ownership and foreign ownership made a positive influence on firm performance and helps in reducing agency costs.
Hastori *et al.*	2015	Indonesia	Sample of 54 firms from 2010 to 2013	Concentration in ownership does not make a significant impact on the agency costs.
Guo *et al.*	2015	Japan	Sample of 322 firms from 2004 to 2008	The negative impact of foreign ownership on profit after inflation of corporate management.
Rashid	2015	Bangladesh	Sample of 110 corporate firms from 2001 to 2011	Tobin's Q – Free cash flow is directly linked with the institutional ownership.
Tahir *et al.*	2015	Pakistan	Sample of 21 firms from 2008 to 2013	Institutional ownership made a direct impact on the financial firm performance and helps in eliminating agency costs.
Songini and Gnan	2015	Italy	Sample of 146 SMEs in the Milan province of Italy	Family engagement in management has a direct and significant impact on agency costs, while family engagement in governance

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Table 1 (Cont.)

Author	Year	Country	Sample	Findings
				has an inverse and significant effect.
Gayan and Shanika	2016	Sri Lanka	Sample of 20 corporate firms	Positive but insignificant influence of institutional ownership on firm performance (return on equity) and hence agency costs.
Masry	2016	Egypt	Sample of 73 firms for eight years	A significant impact of institutional ownership on monitoring and controlling activities of corporate firms and helped in reducing agency conflict.

There is a negative link between foreign institutional ownership as well as institutional ownership and agency costs that are given by the studies (Bhattacharya and Rao, 2005; Xiao and Yuan, 2007; Ajina and Lakhal, 2010; Charfeddine and Elmarzougui, 2010; Liang *et al*., 2011; Benjamin *et al*., 2014; Rashid, 2015; Tahir *et al*., 2015; and Masry, 2016). All the given research studies support Internalization theory, Resource-based theory and Upper Echelon theory. The Internalization theory was developed by Rugman in 1981. This model states that MNCs will provide an advantage by creating their internal market where intra-group transactions can be undertaken at reduced cost and help to enhance profitability. Resource-based theory was propounded by Birger Wernerfelt in the year 1984 that stated that foreign owners tend to possess high caliber human capital under rewarding their talent and expertise in the form of higher remuneration and better perks. They are armed with experience and exposure to global business practices and regulations and able to make optimum utilization of resources of the company for raising productivity and profitability and offer valuable advice to their firms for making cross-border acquisitions. Upper Echelons theory was propounded by Hamrick and Mason in 1984. On the basis of this theory, appointing more foreign directors of different backgrounds, nationalities and religions will bring different perceptions, beliefs, values, experiences, and cognitions to the decision-making way, which ultimately contributes to more rational, mature and efficient strategic solutions.

Some research studies by Uhomoibhi (2007), Fazlzadeh *et al.* (2011), Fauzi and Locke (2012), Miguny *et al*. (2013) and Guo *et al*. (2015) depicted that there is a positive link between institutional ownership and foreign ownership and agency costs. These studies support Agency theory as well as rescue acquisition model. Agency problem generally persists in corporate firms due to separation of ownership from control that could potentially be reduced or eliminated to a certain extent with the principals (shareholders) appointing the board of director to whom agents (managers) report to. If foreign directors are appointed by principals, it weakens

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monitoring efficacy due to long geographical distance from their domiciled economies and foreign directors are not much familiar with the domestic business environment and consumer preferences, so corporate firms with more foreign directors are associated with greater agency problem and ultimately leads to poor firm performance. Rescue acquisition model stressed that poorly performing domestic companies should have more foreign participation that promotes a high degree of foreign ownership. After the financial crisis of Asia in 1997, it was observed that in the emerging markets poorly performing domestic companies were in dire need of capital for survival purposes so they agreed to take lower bid price from acquirers, which means acquisitions by foreign owners.

Concentrated ownership leads to a reduction in agency costs that are shown in many research studies (Anthony and Chinaemerem, 2012; Alexander *et al*., 2014; and Hastori *et al*., 2015).

Agency Costs and Managerial Ownership

Agency costs will be nil in the owner-manager corporate firms, according to Jensen and Meckling, (1976). In the case of public-traded corporate firms, the ownership is separated from the management that will lead to agency costs. Managerial ownership can be treated as an incentive to align the interests of principals with agents. Ang *et al.* (2000) stated that as the shareholdings of agents increase, the misuse of assets and funds by agents will be reduced to a minimum, as agents will be able to take their share in the profitability of corporate firms and their remuneration remains the same. The Table 2 furnishes some empirical research studies showing the link between managerial ownership and agency costs.

Table 2: Impact of Managerial Ownership on Corporate Performance and Agency Costs

Author	Year	Country	Sample	Findings
Fleming *et al.*	2005	Australia	Sample of 3,800 firms from 1996 to 1998	Managerial ownership makes a positive impact in reducing agency costs.
Hua and Zhou	2006	China	Sample of 83 firms from 1998 to 2000	The positive impact of managerial ownership on company financial performance and help in reducing agency costs.
Florackis	2008	The UK	Sample of 897 firms from 1999 to 2003	Executive ownership helps in mitigating the agency costs.
Ahmed	2009	Malaysia	Sample of 100 blue-chip firms from1997 to 2001	The inverse link between managerial ownership and agency costs.
McKnight and Weir	2009	The UK	Sample of 128 firms from 1996 to 2000	The inverse relationship between board ownership and agency costs.

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Table 2 (Cont.)

Author	Year	Country	Sample	Findings
Mustapha and Ahmad	2011	Malaysia	Sample of 235 firms for period 2006	The inverse link between managerial ownership and monitoring costs.
Shahab-u-Din and Javid	2011	Pakistan	Sample of 60 firms from 2000 to 2007	The inverse link between leverage policy and managerial ownership but the direct impact of managerial ownership on corporate performance.
Alfadhl and Alabdullah	2013	Iran	Sample of 27 firms from 2005 to 2008.	The significant but negative impact of managerial ownership on the agency cost of a corporate firm.
Murni	2015	Indonesia	Sample of 123 firms from 2010 to 2013	The direct impact of managerial ownership and institutional ownership on the voluntary disclosure requirements as well as on firm financial performance and helped in reducing agency costs.
Rashid	2015	Bangladesh	Sample of 110 non-financial firms from 2001 to 2011.	Managerial ownership reduces the asset utilization ratio under agency cost.
Noradiva *et al.*	2016	Malaysia	Sample of 46 firms from 2009 to 2012.	Insignificant and nonlinear impact of managerial ownership on intellectual capital performance. The negative impact of managerial ownership on the market value.

Many research studies like Fleming *et al*. (2005), Hua and Zhou (2006), Florackis (2008), Ahmed (2009), McKnight and Weir (2009), Mustapha and Ahmad (2011), Shahab-u-Din and Javid (2011), Alfadhl and Alabdullah (2013), Murni (2015) and Rashid (2015) show that managerial ownership makes a positive impact in reducing agency costs. All the findings of the given research studies support Managerial entrenchment theory. Noradiva *et al*. (2016) depicted contradictory results. The inverse link between managerial ownership and agency costs is found to be an insignificant one. Convergence of interest hypothesis is applied when managerial ownership is between 48.35% and 55.06%. When there is an increase in asset utilization efficiency associated with managerial ownership, that helps in mitigating principal-agent conflicts.

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Agency Costs and Board Structure

Agency theory focuses on fair and sound corporate governance mechanisms that can bring a reduction in the conflicts between principals and agents. Large and strong boards are helpful for firms and they serve as good governance tools (Pearce and Zahra, 1991). Small boards are considered more useful for firms (Lipton and Lorsch, 1992). There are many kinds of governance tools that are used in eliminating agency costs, and in this part, the authors have chosen board size, frequency of board meetings, and board independence. Table 3 explores the empirical studies showing the link of these variables with agency costs.

Table 3: Impact of Board Structure on Corporate Performance and Agency Costs

Author	Year	Country	Sample	Findings
Florackis and Ozkan	2004	UK	Sample of 1,150 UK public listed companies for 1999.	The positive impact of board size and the agency costs because larger boards led to less efficiency and more conflict among the board members.
Truong	2006	Australia	A sample size of 500 companies for 2004.	Insignificant relationship between ownership concentration and board composition and agency costs.
Drakos and Bekir	2010	Greece	Sample of 146 and 232 firms in 2000 and 2006 respectively	Board independence and the leadership structure put an insignificant impact on firm performance but an inverse relationship between board size and firm performance (Tobin *Q*).
Ntim and Osei	2011	South Africa	Sample of 169 firms from 2002 to 2007.	A positive relationship between the frequency of board meetings and firm performance and the capacity of board members for consultation, supervision, and management will become increased when they met regularly through meetings and helps in mitigating agency costs.
Horvath and Spirollari	2012	United States	Sample of 136 firms from 2005 to 2009	Insignificant relationship between firm performance and board meeting frequency.
Aduda *et al.*	2013	East Africa	Sample 98 of companies listed at the Nairobi Securities Exchange.	The relationship between board composition and firm performance (Tobin *Q* and return on assets) was found to

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Table 3 (Cont.)

Author	Year	Country	Sample	Findings
				be significant and contributed to reducing agency costs.
Kumar and Singh	2013	India	A sample size of 176 Indian firms	The positive impact of promoter ownership on the value of the corporate firm and if ownership of promoters exceeds 40%, it will make a positive and significant impact on the value of the corporate firm.
Bertoni *et al.*	2014		A sample size of 969 IPO firms from 1995 to 2011	The link between board independence and firm age is a U-shaped curve because of changes in the roles of the board and the importance of board independence varied with the knowledge intensity of the industry and the age of the listing company.
Alves	2014	Portugal	A sample size of 33 non-financial companies	The positive impact of independent board members on the earnings quality and helps in mitigating agency costs.
Akpan	2015	Nigeria	Sample of 79 companies from 2010 to 2012.	The direct impact of board size, independent directors, board meeting frequency on the firm performance (Tobin *Q* and return on assets).
Adebiyi	2017	Nigeria	Sample of 15 deposit money banks from 2005 to 2016.	The positive impact of financial reporting quality on the board size and board independence and negative impact of financial reporting quality on the frequency of board meetings.
Herdjiono and Sari	2017	Indonesia	A sample size of 156 Indonesian corporates	The positive impact of board size on firm performance but the insignificant impact of the size of the audit committee, institutional ownership, and managerial ownership on the firm performance and finally it concluded that the size of the board, audit committee size,

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Table 3 (Cont.)

Author	Year	Country	Sample	Findings
				institutional ownership, and managerial ownership all made a significant influence on financial performance.
Jehu and Ibrahim	2018	Nigeria	A sample size of 576 firms from 2011 to 2016.	The negative impact of non-executive directors and independent non-executive directors on the abnormal accruals led to making improvements in the quality of financial reporting of a corporate firm but an insignificant relationship between board size and financial reporting quality.
Hanh *et al.*	2018	Vietnam	Sample of 94 firms from 2013 to 2015.	The negative relationship between the frequency of board meetings and firm performance (return on assets, return on equity, and return on sales) and helps in mitigating agency costs.
Shaifali and Mittal	2019	India	Sample of 380 firms, selected based on market capitalization from 2007 to 2012	A positive link between board size and agency costs but the negative association of agency costs with promoter's shareholdings, independent directors, executive directors, duality of CEO/Chairman, audit and shareholders' committees, nomination and remuneration committee, and firm size.

A direct link between board size and agency costs is provided by many research papers (Florackis and Ozkan, 2004; Drakos and Bekir, 2010; and Shaifali and Mittal, 2019). These study findings support Agency model and Stewardship model. The Agency model depicts that a reasonable number of board members should be in the corporate firms to monitor the affairs of the company. More members on the board means conflict of interest among them as well as with principals, which further worsens the firm performance and increases agency cost. The stewardship model stresses smaller board sizes in the corporate firms as the conflict between agents and principals will be reduced because there is lesser number of views and suggestions in the smaller board. If the board has more members, it adds to the cost to the corporate firm in terms of sitting fees and remuneration to the board members, inefficient monitoring, chances

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of manipulation and fraud. If these expenses are more than the profitability of corporate firms, it will contribute negatively to the firm performance.

The findings of the studies do not agree with the Resource-based model. Resource dependency model shows that a larger board brings more chances for more connections to other organizations and thus access to external resources such as legitimacy, advice, and counsel. Despite this, there are certain serious limitations to having larger boards in corporate firms. Eisenberg *et al*. (1998) depicted that larger boards are less feasible and practical. Other major limitations of having more members in the boards involve slow decision making, lack of communication and coordination, conflict of views, and lack of harmony among them that affect the efficacy and effectiveness of the board.

Many research studies like Alves (2014), Bertoni *et al*. (2014), Akpan (2015) and Adebiyi (2017) found that there is a positive link between independent directors and firm performance. These findings of the given studies support the monitoring theory of agency model. Monitoring theory of agency model tells that the inclusion of more independent directors in the board will increase monitoring of management and make them accountable to act in the best interests of the shareholders and other stakeholders. Thus, it helps improve the financial performance of the corporate firm.

There is a positive relationship between the frequency of board meetings and firm performance, so it can help in mitigating agency costs. This conclusion is given by many empirical studies considered (Ntim and Osei, 2011; and Akpan, 2015). Adebiyi (2017) and Hanh *et al*. (2018) found that there is a negative link between frequency of board meetings and firm performance and so the agency costs.

Agency Costs and Firm Structure

Agency theorists are of the opinion that variance in the interests between principals and agents can be eliminated by practicing fair tools of corporate governance. Firm age and firm size make an impact on firm performance and thereby help in reducing agency costs. Table 4 provides empirical works regarding the link between firm age, size with agency costs.

Table 4: Impact of Firm Structure on Corporate Performance and Agency Costs

Author	Year	Country	Sample	Findings
Black *et al.*	2006	Korea	The sample of 534 firms	A positive and significant impact of firm size on the market valuation of a corporate firm and helps in mitigating agency costs.
Papadogonas	2007	Greece	The sample size of 3,035 corporate firms	The positive and significant impact of firm size on the profit rate of corporate firms and thereby helps in reducing agency costs.

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Table 4 (Cont.)

Author	Year	Country	Sample	Findings
Coad *et al.*	2007	Spain	Sample of 73,891 firms from 1998 to 2006	The direct impact of firm age on financial firm performance and thereby helps in reducing agency costs.
Halil and Hasan	2012	Turkey	Sample of 143 firms from 2005 to 2011	The positive impact of firm size on profitability (assets utilization ratio) and helps in eliminating agency costs.
Yinusa and Babalola	2012	Nigeria	Sample of 80 non-financial corporate firms	The negative impact of firm size on the capital structure.
Hui *et al.*	2013	Malaysia	A sample of 168 manufacturing companies in the food industry	A direct and significant impact of firm age on the profitability of corporate firms and helps in declining agency costs.
Akinyomi and Olagunju	2013	Nigeria	Sample of 40 firms from 2005 to 2012	The positive impact of firm size on the profitability of the corporate firm (Tobin *Q*) and helps in reducing agency costs.

Many research studies by Coad *et al.* (2007) and Hui *et al.* (2013) show that there is a direct relationship between firm age and firms' financial performance and ultimately it brings a reduction in agency costs. The given research studies support the 'learning by doing' model, liability of newness model, economies of scale model and financial growth cycle model. Learning by doing model describes that a firm increases its productivity and efficiency as employees do learn about more productive methods and production technology. The liability of the newness model describes how young corporate firms face higher risks of failure as compared to mature and old companies. There is no experience and idea to manage and organize corporate firms so they face higher risks and failures when they are at their infancy stage. Economies of scale model depicts that profitability and low cost can be attained by corporate firms when they are established, mature and big. An enterprise can enjoy cost advantages because of firm age and firm size. The average cost per unit decreases as output increases. The financial growth cycle model reflects the changes in financial needs and financing options with the change in firm size, firm age and information. Mature, established and experienced firms with more transparency help in gaining easy accessibility to public equity or long-term debt financing. The risk of a firm reduces with the age of corporate firms.

The above literature review findings do not support the Structural inertia model and liability of Obsolescence model and liability of Senescence model. Structural inertia theory believes that the growth of corporate firms suffers from administrative blockage and rigidity which may

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modify the problem of resistance to change—conservative dynamics. Established firms are mostly suffering due liability of obsolescence model. It is difficult for established firms to adapt to the changing business environment. The established firm also faces the liability of Senescence model. Old and established firms are rigid in their accumulated rules, routines and organizational structures.

There is a positive link between firm size and corporate financial performance that helps in eliminating agency costs. This result is found in these studies (Black *et al*., 2006; Papadogonas, 2007; Halil and Hasan, 2012; and Akinyomi and Olagunju, 2013). These research studies support the economies of scale model, risk bearing hypothesis, theory of transaction costs. Large firms, based on risk bearing hypothesis, are found to be more capable and having survival ability at the time of recession as they have huge assets. Large firms also have sinking and contingency funds with them to deal with any uncertainty in changing business environment and maintain the minimum existence level. The Theory of transaction costs depicts that when new processes and new methods to solve any problem of corporate firms are discovered, it reduces the transaction costs and opens the avenues to further revenue growth.

Agency Costs and Remuneration Structure

Agency theory describes that there is a conflict in the interests of principals and agents that will bring agency costs. Agents, as hired by principals, are provided remuneration as per Companies Act, 2013 regulation. But there is no information provided for the incentives for efficient and productive agents. No definition is given regarding who is the efficient or not efficient manager. So, it is a usual practice to demand some incentives either in monetary form or higher remuneration or non-monetary benefits are expected by agents that can bring a reduction in agency costs and it will bring corporate financial profitability. Table 5 provides the empirical research studies that focus on the link between remuneration to agents and agency costs.

Table 5: Impact of Remuneration Structure on Corporate Performance and Agency Costs

Author	Year	Country	Sample	Findings
Gregg *et al.*	2005	The UK	A sample size of 415 firms from 1994 to 2002	The high elasticity of pay-performance where stock returns were large and vice versa. Little impact of an executive's pay on corporate financial performance.
Abdullah	2006	Malaysia	A sample size of 172 firms of period 2001	The negative impact of the director's remuneration on firm performance but the direct impact of firm size and firm age on the director's remuneration.

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Table 5 (Cont.)

Author	Year	Country	Sample	Findings
Zhu *et al.*	2009	China	Sample of 362 firms from 2001 to 2004 and 492 firms from 2005 to 2007.	The positive impact of independent board members on the executive pay performance but an insignificant relationship between the independence of compensation committees and executive pay performance.
Herdan and Szczepanska	2011	UK	Sample of 50 from 2007 to 2010.	The positive correlation between directors' remuneration and the size of firms and the direct impact of directors' pay on corporate financial performance (return on equity and Tobin's *Q*).
Scholtz and Smit	2012	South Africa	Sample of 58 firms from 2003 to 2010	The strong and significant impact of executive remuneration on the company's financial performance and help in eliminating agency costs.
Miyienda *et al.*	2013	Kenya	Sample of 57 firms from 2006 to 2010	A strong impact of the director's remuneration on the raw performance indicators and points out the aggravation of agency problem as directors were benefitted from raw earnings and there was no link between market performance and long-term performance.
Aggarwal and Ghosh	2015	India	Sample of 40 companies	The direct impact of the director's remuneration on corporate performance as per accounting reference.
Raithatha and Komera	2016	India	Sample of 3,100 firms from 2002 to 2012.	A significant impact of executive compensation on firm performance but no link between the pay-performance of smaller corporate firms and big business corporate firms.
Njuguna	2016	Kenya	Sample of 20 financial services firms from 2003 to 2013	Insignificant impact of board remuneration on return on assets, EPS, and return on equity and a significant impact of board remuneration on the

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Table 5 (Cont.)

Author	Year	Country	Sample	Findings
				return on assets in the insurance sector but no significant impact of board remuneration on corporate financial performance in the investment sector.
Razali *et al.*	2018	Malaysia	Sample of 40 companies from 2012 to 2014	The direct impact of the director's remuneration on firm performance and high remuneration was considered as an incentive tool for directors and it will help in reducing agency cost.
Md Zin *et al.*	2019	Malaysia	Sample of five corporate firms from 2013 to 2017	The negative impact of the director's remuneration and board size on firm financial performance. The negative impact of larger board size on the corporate financial performance as it is difficult to perform monitoring efficiently.

There is a little but negative impact of director's remuneration on corporate performance and thereby on agency costs. This conclusion is provided by research studies like Gregg *et al*. (2005), Abdullah (2006), Zhu *et al*. (2009), Njuguna (2016) and Md Zin *et al*. (2019).

The findings of many research studies of Herdan and Szczepanska (2011), Scholtz and Smit (2012), Aggarwal and Ghosh (2015), Raithatha and Komera (2016) and Razali *et al*. (2018) show that there is a direct and significant link between executive compensation and firm performance and thereby it helps in mitigating agency costs.

Conclusion

This paper focused on the worldwide literature on the essential aspects of agency theory. The deliberation on agency relationship and variance in the interests of principals and agents began with Adam Smith in his book, *The Wealth of Nations* published in 1776 and continues till the present day. The engrossing task of outstanding agency theory, by whom the agency problem was conjectured, has described the principal-agent issue in different forms.

These brilliant works of literature have directed us to demonstrate the link between tools of corporate governance and agency costs. This also provides solutions to the questions that revolved around the Agency theory as well as agency costs. Through this review of literature on agency costs and tools of corporate governance, it can be summed up that this is a very practical and applied theoretical foundation.

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Agency theory has connections in several different academic disciplines and its significance is all-pervasive and well known. Many academicians have pointed out that agency problem exists in every type of organization except which are managed by owners themselves. It inspired many researchers, academicians and students to make extensive literature reviews and conduct different empirical studies on agency problem, which cover different countries and explore the solution for mitigating agency costs which arise due to the conflicting interests of both principals and agents. Many researchers have concluded that separation of ownership from management, variance in interests, information asymmetry, and risk averseness are the main reasons for agency problem, while it was found that board composition and ownership, shareholding pattern, firm structure (firm age, size, and firm growth) and managerial ownership all can mitigate the agency costs. There are certain gaps found through literature review and these may be taken up in future studies on Agency theory.

Relevance of the Study: In a developing country like India, there is a need for extensive review of literature regarding ownership structure, board structure, firm structure, managerial ownership, and remuneration structure that can make an influence on firm performance. Corporate governance is a popular topic in developed nations, but in India, this issue got recognition only after new economic reforms. Still, India lacks good research studies that depict the link between corporate governance mechanisms and corporate financial performance that ultimately will reduce agency costs. This study has depicted that tools of corporate governance make a direct and positive impact on firm performance and it also helps in eliminating agency costs. Almost all the reviewed works have provided this evidence. This theoretical foundation related to tools of corporate governance and agency costs has important implications for the research scholars, academicians, company directors, and policymakers who are engaged in framing different rules and guidelines for corporate governance in emerging countries like India. The conclusions provided based on extensive review of literature show that corporate firms that comply with sound corporate governance frameworks can expect to attain improved financial performance and help in mitigating agency costs. Hence, policy framers may be able to provide an appropriate contribution to the efficient functioning of the country by making optimal guidelines for corporate governance. These kinds of reviews stress that to attain sound and efficient standards of corporate governance, the policymakers should focus on the tools of corporate governance that make a direct impact on firm performance, and also these serve in mitigating agency costs. This study collectively shows all tools of corporate governance and their impact on mitigating agency costs.

Limitations of the Study:

- It is seen that literature reviews have mainly stressed the principal-agent problem and there is a scarcity of research studies on the kinds of agency problems like principal-principal problems and principal-creditor problems.
- It is seen that there are very few research studies conducted on the agency costs and the reasons that eliminate the agency costs.

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- Generally, research studies on agency costs and corporate governance mechanisms were focused on developed and developing countries like the US, the UK, India, Pakistan, and a few for less developing countries.
- Research studies on the agent-agent problem were not seen and it can be a relevant and popular area for future research study in the Agency theory.
- It is not possible to make a comparison between the studies of developed and developing countries as there are very few studies done in emerging economies.
- The review of literature tries to cover all the links between corporate governance tools and agency costs but their availability is limited to online databases.
- The aspects and issues that were highlighted and covered in this paper might not be the whole issue of the Agency theory.
- Despite these shortcomings, this literature review will assist the research scholars, academicians and policymakers in analyzing the problem of principal-agents and constructing empirical models in their future research studies.

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