A note on the efficacy of the current corporate governance regulations in India.

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ABSTRACT

Unlike the central governance issue in the Anglo Saxon world, which is essentially that of disciplining management that may stop being accountable to the owners, who usually are dispersed shareholders, the central challenge in corporate governance in India is that of disciplining the dominant shareholder and protecting the interest of the minority shareholders.

Besides family ownership, other forms of domination, such as domination by government or a foreign group, also exist in Indian organizations. Additionally, often promoters of companies exercise influence that is disproportionate to their actual shareholding.

Our study finds that differences in the nature of the dominating shareholder(s) result in significant differences in the firm's corporate governance characteristics and in firm performance. These differences lead to serious doubts on the efficacy of a uniform, prescriptive corporate governance code –as is being attempted in India.

The need for deeper research, leading to fresh insights that would help in developing a more effective policy for corporate governance, is emphasized.

Key Words: Corporate Governance, India, Dominant Shareholder, Firm performance.

I. Introduction

As early as 1776 Adam Smith had argued that the separation of ownership and control in publicly held corporations created poor incentives for professional managers to operate the firm efficiently and the performance of the firm was likely to suffer– the first articulation of the agency problem.

Corporate governance deals with the agency problem and has been defined by Shleifer and Vishny (1997) as '… how to assure financiers that they get a return on their investment'. While worldwide, investors prefer to invest in companies with good corporate governance, Coombes and Watson (2000), there no unanimity on what constitutes good governance and there is considerable divergence on this subject.

Some empirical studies have found different measures of 'good' governance to be positively correlated with firm performance, Gompers, Ishii and Metrick (2003), Bebchuk, Cohen and Ferrell (2004) Brown and Caylor (2004) and based on such results it has been the objective of policy makers, across the world, to attempt a change the governance characteristics of the firm towards a desirable standard, based on an intuitive belief that 'better' governance, will result in an improvement in the firm's performance.

Steps taken in India for better corporate governance, while of recent origin, have largely followed the prescriptive approach. The introduction of a common, desirable code of corporate governance through the clause 49 of the Listing Agreement, prescribed by the Securities and Exchange Board of India, (SEBI) for listed companies, has been followed by incorporating several corporate governance prescriptions in the new Companies Bill, 2012 making the prescriptive approach to corporate governance applicable to all companies.

While the elusive search for a universal standard of 'good governance', towards which all firms are expected to strive towards, has been a major goal of corporate governance research, some researchers have suggested that good governance is best understood as being highly context-specific and the most effective governance system would depend on the context of the firms' specific circumstances, making it very difficult, almost impossible, for a prescription based approach to capture the nuances of what constitutes good governance, Bebchuk & Hamdani(2007),Khanna (2009), Arcot and Bruno (2007), Bhagat, Bolton and Romano (2008),Van den Berghe and Levrau (2003).

This paper examines how feasible is it to have a prescription based common code for corporate governance in India and is organized as follows- Section II briefly describes the evolution of corporate governance in India and identifies India specific parameters that impact corporate governance and which need to be taken into account while drawing up corporate governance policy , section III defines the framework of this investigation, the parameters used in the study and describes the source of our data, section IV summaries the results and the conclusions from the study while section V examines the policy implications of our findings and suggests the plan of action for the future.

II. **Corporate Governance in India.**

Since financial liberalization began in 1991 in India, the country has undergone significant corporate governance reforms. While, on paper, the framework of India’s legal system provides some of the best investor protection in the world, enforcement is a major problem with slow, over-burdened courts and significant corruption. Despite the challenges, corporate governance in India does not compare unfavorably with any of the other major emerging economies and if the trend of corporate governance reforms was maintained then India should have the quality of corporate governance necessary to sustain its impressive current growth rates, Chakrabarti, Megginson, and Yadav, (2007), Pande (2011).

Pointing out that unlike the governance issue in the US or the UK which is essentially that of disciplining the management, who has ceased to be effectively accountable to the owners, the central problem in the Indian corporate sector is that of disciplining the dominant shareholder, who is the principal block holder, and of protecting the minority shareholders, Varma (1997) has argued that the corporate governance problems in India are very different from those found in the Anglo Saxon World and fixing these would need a different model for corporate governance - one that would have a significant external focus.

While family managed organizations dominate the private sector in Indian Business, Bajaj (2004), Godrej (2005), other dominant groups, like the public sector units (PSUs) where the government is the dominant (in fact, majority) shareholder and the multinational companies (MNCs) where the foreign parent is the dominant (in most cases, majority) shareholder, also exist, Varma (1997) .

Through surveys, conducted across Indian organizations, researchers have found that, despite a few notable companies, important governance issues persist among India companies, Banaji and Mody (2001), Mukherjee & Ghosh (2004), ICRA (2007): however positive relationship between corporate governance practices and firm performance in India have been reported by Black & Khanna (2007),Balasubramanian, Black and Khanna (2008), Mani and Sridharan (2004).

Anecdotal evidence from Indian Business has clearly bought to the forefront the challenges to corporate governance and role of the dominant shareholder in undermining good governance. Chronicling the dispute in the Ambani family, Dalal (2005) has pointed out, ironically, that the serious charges of mis-governance were levied against a company that had been showered with awards of Corporate Excellence (Institute of Company Secretaries) in 2003 and Corporate and Social Responsibility awards (Golden Peacock, by the Institute of Directors) in 2004 which actually coincided with the period when the alleged misdemeanors had actually taken place!
The accounting scandal (in January 2009) involving Satyam Computer Services (Satyam) was India’s ‘Enron moment’ that demanded a reassessment of the country’s progress in corporate governance, India’s Enron? (2009) and pointed to the key role played by the promoter (as the dominant shareholder) even in a situation where he did not have majority control.

Notwithstanding the recent approval of the new Companies Bill by both houses of the Indian parliament (the introduction of which is widely believed to provide a strong boost to the movement for better corporate governance in India), corporate governance reforms in India currently are at crossroads; while there is no doubt about the good intention behind the reforms, there is a need to look for a more complete solution, evolved from within, and to craft a solution that would address the specific challenges of India and the evolution of home grown solutions to address the corporate governance challenges in India, Varottil (2009).

III. Framework for the Study, parameters investigated, sample used for the study and source of data.

Most of the empirical corporate governance research, in India, do not take adequately into account factors and conditions that are specific to Indian firms with the result that the relationships between corporate governance parameters and the value of a firm are not properly explained and, very often, these relationships are not adequately tested by incorporating the relevant factors affecting them. For instance, one such key factor of importance that is not fully explored in prior research is the qualitative dimension of ownership concentration which, in the Indian context, is characterized by the nature of the dominant shareholder(s).

The primary motivation for this study is to carry out an India specific study of corporate governance in organizations that would examine whether the differences in the nature of the dominant shareholder(s) in Indian business organizations significantly impact corporate governance in organizations and whether differences exists in the performance of firms with different dominant shareholder(s).Arising from our findings, the policy prescription on the efficacy of having a common code for corporate governance for Indian companies is also discussed

Researchers, while examining the governance framework of Indian companies, have attempted to identify the constituents of corporate governance, use them to build an overall index to measure governance and then develop a regression model of the index and its constituents with firm performance; Balasubramanianm et al (2008), Mohanty (2002),Selarka(2005).

Such empirical research can be faulted on two counts, firstly no one index can predict a firm's performance on all of the performance measures that are thought to be important to investors and secondly, and more importantly, such indices are constructed so as to treat the various components that constitute the governance mechanisms as complements, whereas data suggest that several of such mechanisms are actually substitutes for, and not complements to, each other, Bhagat et al (2008)

Agreeing with the view that,' one size indeed does not fit all' and that good governance is best understood as being highly context-specific, in this study an attempt is made to identify select India specific, key underlying factors that impact governance (and are amenable to measurement) and using them as proxies for governance in the study, examine the differences in corporate governance characteristics and firm performance for Indian firms that are grouped on the basis of the nature of the dominating shareholder(s).

Structures, institutions, and legal framework of corporate governance are developed and administered by individuals whose behaviors are shaped by cultural factors and personal beliefs as well as by the social environment in which they function; problems are expected to arise when the prevailing influences do not conform to the regulatory prescriptions that are sought to be enforced (through prescriptive legislation) for better corporate governance. In such a situation, the factors that would have the greatest impact on governance would be those where the clash between prevailing culture, social ethos, personal beliefs and the external governance regulations are expected to be the strongest; these would also be the right indicators for measuring the effectiveness of governance. In the Indian business context such clashes are expected to be the strongest in three areas: related-party transactions, the promoter's or large shareholder's actions, and the board's nominations, deliberations, and effectiveness, Kar (2011).

Also, given that the problem in the Indian corporate sector (be it the public sector, the multinationals or the Indian private sector) is that of disciplining the dominant shareholder and of protecting the minority shareholders; Varma (1997), it follows that the nature of dominant shareholder(s) in the organization would be a key variable in any investigation into corporate governance and firm performance.

Three key governance parameters are taken up, for investigation, in this study to define corporate governance for the Indian firms; these relate to the nature and functioning of the board, the independence of the auditors and the amount of self dealing transactions that an organization does with its related parties. Since the nature of the dominant shareholder is a key factor in the Indian context, that is likely to have a significant impact on corporate governance and firm performance, it is examined as the fourth parameter in our study. Firm performance, is the fifth parameter in the study and is measured, by Tobin's Q and Return on Assets (ROA)

The investigation into the nature and functioning of the board involves an enquiry into the various elements of board governance, such as board size and composition, frequency of board meetings and participation of independent directors (collectively referred to as **Board Structure and Process**) as they relate to financial performance, Shleifer and Vishny(1997)

An independent board of directors in public listed companies is seen as an integral element of a country's corporate governance norms and board independence has taken on a pivotal status in corporate governance that it has become almost indispensable. Consequently, recent governance reform measures (in particular, the proposed Companies Bill, 2013) have pinned hope, as well as responsibility, on independent directors to enable higher standards of governance; for instance the concept of an Independent Director has been defined and all listed companies are required to appoint independent directors with at least one-third of the board of such companies comprising of independent directors.

In analyzing the governance role of Independent Directors on company boards' two key variables of interest are;

i. the independence of the Board i.e. extent to which independent directors constitute the board of the company and,

ii. the diligence of the Independent Directors i.e. extent to which independent directors are diligent in their duties.

While (i) would proxy the independence of the board from the influence of the dominant shareholder(s) -the Index of Independence, (ii) -the Index of Diligence would be a proxy for the quality of monitoring by independent directors.

Our study follows the commonly used approach, popular in empirical studies, of measuring the board's Index of Independence by the proportion of independent directors on the board to the entire number of Board members of the firm and measuring the Index of Diligence of the board as the actual attendance by Independent Directors is Board meetings expressed as percentage of total number of Board meetings that the Independent Directors were expected to attend.

We determine an overall Board Structure and Process Index by multiplying the Independence Index with the Diligence Index and expect that a higher value for this index, as manifested in an independent and diligent Board, will be positive for the firm's corporate governance process.

Independence of Auditors has been an area of extensive research in accounting literature and studies in this genre have looked at the effect auditor independence on earnings management, earnings in formativeness, and other measures of earnings quality, Sarkar & Sarkar (2010). Theory and the empirical literature suggest that auditor and audit committee independence play an important role in the governance of companies, Frankel, Johnson and Nelson (2002), Ashbaugh, La Fond and Mayhew (2003), Larcker and Richardson (2004), Mishra and Raghunandan (2007).

We develop an Index for Auditor's Independence by calculating the ratio of audit fees paid by the firm to its Auditors to the total fees paid to the Auditors (for all services rendered to the firm) as a proxy to measure the independence of Auditors. A higher level for this Index (maximum of 100%) indicates that the Auditor provides primarily Audit services since, at the 100% level for this Index, there is no engagement with the firm in providing any non audit related work and is taken as an indicator for good governance. At lower levels of Index, the auditor's engagement with the firm for providing non audit services increases and there is a greater share for non audit service engagement making the auditor more dependent on the company for their economic survival which could, possibly, hinder and compromise the ability of the Audit Firm to fully and faithfully discharge its audit related functions.

Related Party transactions (RPTs) and other forms of self-dealing transactions by controlling shareholders are a significant concern in India where most firms have a major, often controlling shareholder, Kar (2011). In their survey Balasubramanian et al (2008) found that while a majority of the firms had policies requiring RPTs to be on arms-length terms, not only approvals of related party transactions by non-conflicted directors uncommon but also approvals by non-conflicted shareholders even rarer.

On one hand, the occurrence of related party transactions in a firm (with other related parties) provides the dominating shareholder with an opportunity to gain private benefit at the expense of the minority shareholders with higher incidence of related party transactions providing greater opportunities for such actions, Gordon, Henry, and Palia (2004) while, on the other hand, there is the opposing view that such transactions are 'efficient transactions' that fulfill rational economic demands of a firm such as the need for service providers with in-depth firm-specific knowledge, Khanna and Palepu (2000).

With increased ownership concentration, the positive impact of any convergence in the interests and identity of the dominating shareholder could be outweighed by the negative impact of management entrenchment and the controlling shareholders might then maximize their private benefits, at the expense of other shareholders, Bhaumik, and Gregorious (2009) ; the extent of this expropriation – popularly referred to as 'tunneling' – is especially high in countries that have weak legislative protection of the rights of the minority shareholders. Bertrand, Mehta and Mullainathan (2002) have reported evidence of tunneling during 1989-1999 within Indian business groups; however, Siegel and Choudhury (2010) failed to confirm this for 1989-2008 period.

Our study examines the Related Party transactions based on only the expropriation of cash flow rights and we develop an Index of Related Party Transactions for the firms, in our sample, in respect of transactions involving purchases from and sales to all the related parties (as defined by accounting Standard AS-18 prescribed by The Institute of Chartered Accountants of India) by calculating the total related purchases from/sales to all related parties as a percentage of the total expenses and sales by the firm for the same period.

The Index ranges from 0 (for a firm that has no related party transactions) to close to 100 (for a firm which has only related party transactions). A high value for the related party index would indicate a higher proportion of related party transactions thereby presenting increased opportunities for tunneling and transferring profits and expenses in a way such that the dominating shareholders controls cash flow disproportionate to their ownership in the firm and thereby serve as an indicator for poor corporate governance practices.

The fourth parameter in our study is the **nature of the dominant shareholding**. Extending the framework proposed by Varma (1997), our study classifies Indian firms into organizations on the basis of difference on account of the nature of ownership by adding a fourth category i.e. dispersed organizations with no dominating shareholders, organizations where no group is identified as the promoter group to the three groups of dominant shareholders identified by him i.e. family, foreign ownership and government.

Finally, **firm performance**, in our study, is measured by Tobin's Q and Return on Assets (ROA); Demsetz and Lehn (1985), Pant and Pattanayak (2007). The decision to use the two measures of financial performance is based on two main reasons -firstly, prior evidence suggests that insiders and outsiders value corporate governance differently; while the accounting based measure of performance (ROA) attempts to capture the wealth effects of corporate governance mechanisms from the perspective of company management (insiders), the market based measure (Tobin's Q) represents financial valuation of corporate governance structures by investors (outsiders). Secondly, both measures have their own strengths and weaknesses with no consensus within the literature on a particular measure as being the 'best' proxy for financial performance.

Our primary hypotheses are that we expect significant differences in the firm's governance characteristics based on the nature of the dominant shareholder(s). We further expect that firms, where the dominating shareholder(s) are expected to have a clearer business focus (for example a firm dominated by a foreign group), could be expected to outperform (as measured by Tobin's Q and ROA) firms that have other forms of dominant ownership.

Our study is based on the sample of S&P CNX 500 companies for three financial years 2009-10, 2010-11 and 2011-12 and data is obtained from the Prowess database maintained by the Center for the Monitoring of Indian Economy (CMIE). Only the firms that constitute the S&P CNX 500 index are included in the sample for this study; this Index represents about 95% of the free float market capitalization of the stocks listed on NSE.

After eliminating data sets where some of the data elements were missing we had 1390 firm-years of data (over three years 2009-12) which was used in our analysis.

IV. Results and interpretation.

Based on the nature of dominant shareholding, the companies in the study have been categorized (by numbers and by market capitalization) in Tables 1 and 2 below;

Table 1- Classification of sample companies –by numbers

Serial No.	Nature of Dominant Shareholder(s)	2010		2011		2012	
		Nos	%	Nos	%	Nos	%
1	Government	41	9.2%	48	10.1%	42	8.9%
2	Indian Business Groups	337	74.7%	351	74.3%	358	76.2%
3	Foreign Business Groups	58	13%	62	13.1%	58	12.3%
4	No Dominating Group	11	2.5%	12	2.5%	12	2.6%
	TOTAL	447	100%	473	100%	470	100%

Table 2- Classification of sample companies –by market capitalization (Rs million)

Sl No	Nature of Dominant Shareholder(s)	2010		2011		2012	
		Market Cap	**%**	**Market Cap**	**%**	**Market Cap**	**%**
1	Government	11,979,618.41	24.45 %	15,904,095.79	27.1 %	12,601,368.45	25.72 %
2	Indian Business Groups	27,932,830.69	57.00 %	31,014,346.65	53.00 %	27,819,776.42	56.77 %
3	Foreign Business Groups	4,833,900.26	9.86%	5,419,524.46	9.3%	5,637,634.04	11.51 %
4	No Dominating Group	4,255,161.30	8.68%	6,190,177.65	10.6 %	5,261,162.85	10.74 %
	TOTAL	44,746,349.36	100%	58,528,144.55	100%	51,319,941.76	100%

While, by numbers, companies with dominating Indian groups constitute more than 74% of the number of companies in the sample under study, they account for only around 53-57% of the total market capitalization of the sample. On the other hand, Government dominated companies (that comprise of only between 9-10% of the number of companies in the sample) account for as much as 24-27% of the total market capitalization of the sample.

Corporate governance has been proxied, in this research, by constructing three indices – board structure & process, index of auditor independence and index of related party transactions.

Table 3 below provides the mean value and standard deviation of the board structure and process index for the period 2010-2012 for the companies in the various groups, based on the nature of dominating shareholder(s), for the S&P CNX 500 companies.

Table 3 - Board structure & process (BSP) index of sample companies

Serial No.	Nature of Dominant Shareholder(s)	2010		2011		2012	
		Mean	**SD**	**Mean**	**SD**	**Mean**	**SD**
1	Government	.26	.11	.26	.13	.25	.13
2	Indian Business Groups	.35	.10	.36	.10	.37	.10
3	Foreign Business Groups	.29	.09	.31	.09	.32	.09
4	No Dominating Group	.42	.16	.38	.18	.44	.22
	Average- S&P CNX 500 cos.	.33	.11	.35	.11	.35	.11

A higher value of the BSP Index indicates a relatively independent and more diligent board where the independent directors are more regular in attending the board meetings, with a theoretical maximum figure of 1.0 reflective of a completely independent board where the directors attend all the board meetings.. Not surprisingly, companies with no dominating shareholders reflected the best value for this indicator indicating that they had more diligent and independent boards as compared to companies in other categories.

Table 4 below provides the mean value and standard deviation of the Index of auditor independence for the period 2010 -2012 for the companies in the various groups, based on the nature of dominating shareholder(s), for the S&P CNX 500 companies.

Table 4 -Index of auditor independence of sample companies.

Serial No.	Nature of Dominant Shareholder(s)	2010		2011		2012	
		Mean	**SD**	**Mean**	**SD**	**Mean**	**SD**
1	Government	73.84	25.59	70.06	25.89	69.00	25.89
2	Indian Business Groups	73.81	18.70	72.70	18.99	74.39	18.11
3	Foreign Business Groups	71.13	19.18	72.74	18.08	73.44	16.10
4	No Dominating Group	85.55	22.42	80.59	25.91	83.11	24.67
	Average- S&P CNX 500 cos.	73.75	19.61	72.64	19.85	74.01	18.93

The maximum level for the index of auditor independence (100) is indicative of a truly ‘independent’ auditor who does not engage in any non audit related work with the company and whose engagement is confined purely to providing audit related services to the company. On this parameter we find the auditors in companies that do not belong to any dominating group to be relatively more independent as compared to the auditors of companies in other categories.

Table 5 below provides the mean value and standard deviation of the Index of related party transactions for the period 2010-2012 for the companies in the various groups, based on the nature of dominating shareholder(s), for the S&P CNX 500 companies.

Table 5- Index of related party transactions of sample companies

Sl No.	Nature of Dominant Shareholder(s)	2010		2011		2012	
		Mean	SD	Mean	SD	Mean	SD
1	Government	2.13	5.73	2.71	6.54	3.63	9.37
2	Indian Business Groups	8.64	12.62	11.10	16.60	10.71	15.26
3	Foreign Business Groups	12.84	12.52	12.24	10.52	13.49	11.27
4	No Dominating Group	3.45	6.23	4.46	8.39	8.54	22.36
	Average for S&P CNX 500 cos.	8.46	12.27	10.23	15.24	10.36	14.75

A higher level of the Index of Related Party transaction is indicative of a higher level of dealings with group companies and associates and, unless controlled, provides an opportunity for tunneling of profits to/from group companies. Not unexpectedly we find that index of related party transactions is higher for companies that have foreign business groups and Indian business groups as their dominating shareholders.

Table 6 below provides the mean value and standard deviation of firm performance (measured by Tobin’s Q) for the period 2010-2012 for the companies in the various groups, based on the nature of dominating shareholder(s), for the S&P CNX 500 companies, while Table 7 below provides the mean value and standard deviation of firm performance (measured by Return on Assets) for the period 2010-2012 for the companies in the various groups, based on the nature of dominating shareholder (s), for the S&P CNX 500 companies.

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Table 6-Firm Performance (measured by Tobin's Q) of sample companies

Sl No.	Nature of Dominant Shareholder(s)	2010		2011		2012	
		Mean	SD	Mean	SD	Mean	SD
1	Government	.88	1.13	1.34	1.15	1.18	1.02
2	Indian Business Groups	1.61	2.00	1.74	1.63	1.53	1,63
3	Foreign Business Groups	2.56	1.85	2.76	1.89	2.92	2.69
4	No Dominating Group	.87	1.27	1.5	1.28	1.56	1.47
	Average for S&P CNX 500 cos.	1.57	1.59	1.82	1.66	1.67	1.80

Table 7 -Firm Performance (measured by ROA) of sample companies

Sl No.	Nature of Dominant Shareholder(s)	2010		2011		2012	
		Mean	SD	Mean	SD	Mean	SD
1	Government	4.35	6.10	4.82	6.29	5.49	7.47
2	Indian Business Groups	7.36	7.19	7.00	7.14	5.64	7.98
3	Foreign Business Groups	11.84	8.87	12.04	9.30	8.96	11.71
4	No Dominating Group	4.54	5.91	4.47	6.00	4.4	6.52
	Average for S&P CNX 500 cos.	7.44	6.74	7.37	7.59	6.00	8.50

The performance of firms that are dominated by foreign groups and Indian groups is consistently better as compared to the performance of companies that have Government as the dominating group. This could be attributed to the sharper focus in foreign group and Indian group dominated firms towards firm performance.

Tables 3-5 above give the mean values for the key corporate governance parameters (board structure & process, index of auditor independence and index of related party transactions), across the four groups of companies ,categorized based on the nature of the dominant shareholder (s), and the next step in investigation was to test whether the differences, in the corporate governance parameters (across the groups), were statistically significant. Likewise Tables 6 and 7 reflect the mean value of the firm performance (measured by Tobin's Q and ROA) across companies in different categories, classified based on the nature of dominating shareholder (s), and it needed to be examined whether the differences in the two firm performance parameters were significant across the four categories of firms.

However, prior to running any statistical tests of significance to check whether or not the differences across the four groups are statistically significant or not, the data (for the years 2010-2012) on corporate governance parameters (board structure and process, auditor's independence and index of related party transactions) and firm performance was tested for normality and it was observed that the results from both the Kolmogorov –Smirnov Test and the Shaprio -Wilk Test were significant at $p<0.05$ level indicating that these parameters were not likely to conform to a normal distribution. Since the study uses 'real world' data, where companies are expected to gravitate towards desired financial norms/objectives, the parameters are, more likely than not, expected to follow a skewed or other forms of non-normal distribution.

The non parametric nature of the data is not surprising; yet we made no attempt to normalize the data or even remove the outliers. While the transformation of the variables (to linear forms) was a possible course of action, this option was not considered as such transformations are usually accompanied by a serious loss of the ability to interpret the results meaningfully, De Coster (2001).

The non parametric one way ANOVA test, the Kruskal Wallis (KW) Test across k samples, was applied to evaluate whether the differences among the companies in the four groups in respect of the three corporate governance parameters and the two firm performance parameters was significant. Testing for significance was done for each of the three years using the asymptotic method as well as the monte - carlo method.

The year wise results from the KW Test are presented in Tables 6-8.

Table 6- KW Test-year 2010- Test Statistics[a,b]

			Board Structure & Process	Index of Auditor Independence	Index of Related Party Transactions	Tobin's Q	Return on Assets
Chi-Square			42.095	6.666	69.851	53.673	30.971
df			3	3	3	3	3
Asymp. Sig.			.000[c]	.083	.000[c]	.000[c]	.000[c]
Monte Carlo Sig.	Sig.		.000[d]	.076[d]	.000[d]	.000[d]	.000[d]
	99% Confidence Interval	Lower Bound	.000	.069	.000	.000	.000
		Upper Bound	.000	.083	.000	.000	.000
a. Kruskal Wallis Test							
b. Grouping Variable: Nature of Ownership							
c. Significant at p<.05 level							
d. Based on 10000 sampled tables with starting seed 2000000.							

Table 7- KW Test-year 2011- Test Statistics[a,b]

			Board Structure & process	Index of Auditor Independence	Index of Related Party Transactions	Tobin's Q	Return on Assets
Chi-Square			42.414	3.178	66.803	46.476	31.526
df			3	3	3	3	3
Asymp. Sig.			.000[c]	.365	.000[c]	.000[c]	.000[c]
Monte Carlo Sig.	Sig.		.000[d]	.363[d]	.000[d]	.000[d]	.000[d]
	99% Confidence Interval	Lower Bound	.000	.351	.000	.000	.000
		Upper Bound	.000	.375	.000	.000	.000
a. Kruskal Wallis Test							
b. Grouping Variable: Nature of ownership							
c. Significant at p<.05 level							
d. Based on 10000 sampled tables with starting seed 2000000.							

Table 8- KW Test-year 2012- Test Statistics[a,b]

			Return on Assets	Tobin's Q	Board structure & Process	Index of Auditor Independence	Index of Related Party Transactions
Chi-Square			16.380	47.722	48.600	5.924	61.200
df			3	3	3	3	3
Asymp. Sig.			.001[c]	.000[c]	.000[c]	.115	.000[c]
Monte Carlo Sig.	Sig.		.001[d]	.000[d]	.000[d]	.114[d]	.000[d]
	99% Confidence Interval	Lower Bound	.000	.000	.000	.106	.000
		Upper Bound	.001	.000	.000	.122	.000

a. Kruskal Wallis Test
b. Grouping Variable: Nature of ownership
c. Significant at p<.05 level
d. Based on 10000 sampled tables with starting seed 2000000.

The summarized output for the Kruskal–Wallis test for the years 2010-2012 is presented in Table 9 below;

Table 9- KW Test-years 2010-2012- Test Statistics [a,b,c]

Serial No.	Corp Gov characteristic	2010	2011	2012
1	Board Structure& Process	.000*	.000*	.000*
2	Index of Auditor Independence	.083	.365	.115
3	Index of Related Party Transactions	.000*	.000*	.000*
4	Tobin’s Q	.000*	.000*	.000*
5	ROA	.000*	.000*	.000*

a. KW Test
b. Significant at $p < 0.05$ level;
c. Grouping Variable: Nature of dominant shareholder ownership.

While the differences in the characteristics of board structure and process and the index of related party transactions are significant across the four categories of firms ,classified on the basis of the nature of dominant shareholder (s), no significant difference exists in respect of the index of auditor’s independence across the four firm categories. Additionally, significant difference was observed in firm performance (measured by Tobin's Q & ROA) across the four categories of firms.

Furthermore, as reported in Tables 6 to 8, the Kruskal Wallis Test, conducted using the monte carlo method (based on 10,000 sampled tables), also gave similar results as the asymptotic test.

As a post hoc study, the above analysis was extended by conducting a pair wise KW test to identify significant difference on corporate governance and firm performance indicators between groups ,based on the nature of dominant shareholder(s), taken two at a time. A total of $^4C_2$ combinations (=6) are possible (for pair wise comparisons) and the post hoc analysis was conducted for all possible six combinations of categories for the three corporate governance variables and two firm performance variables across the three years.

The findings, on whether or not the pair wise differences are significant (at p<0.5 level), are summarized in Table 10 below.

Table 10- KW Test –years 2010-2012- comparing corporate governance and firm performance parameters across firm categories (taken two at a time)

Sl No	Comparison across the following categories		2010	2011	2012
1	Government dominated firms and Indian group dominated firms	Board Structure& Process	.000*	.000*	.000*
2		Index of Auditor Independence	.653	.691	.304
3		Index of Related Party Transactions	.000*	.000*	.000*
4		Tobin’s Q	.000*	.005*	.476
5		ROA	.002*	.199	.429
6	Government dominated firms and Foreign group dominated firms	Board Structure& Process	.095	.030*	.002*
7		Index of Auditor Independence	.296	.868	.417
8		Index of Related Party Transactions	.000*	000*	.000*
9		Tobin’s Q	.000*	.000*	.005*
10		ROA	.000*	.000*	.000*
11	Government dominated firms and firms with no dominating groups	Board Structure& Process	.001*	.045*	.006*
12		Index of Auditor Independence	.249	.240	.098
13		Index of Related Party Transactions	.042*	.024*	.478
14		Tobin’s Q	.858	.542	.596
15		ROA	.466	.459	.084
16	Indian group dominated firms and Foreign group dominated firms	Board Structure& Process	.000*	.000*	.000*
17		Index of Auditor Independence	.305	.925	.515
18		Index of Related Party Transactions	.000*	.002*	.001*
19		Tobin’s Q	.000*	.000*	.000*
20		ROA	.000*	.000*	.000*
21	Indian group dominated firms and firms with no dominating groups	Board Structure& Process	.127	.672	.291
22		Index of Auditor Independence	.021*	.076	.031*
23		Index of Related Party Transactions	.042*	.913	.018*
24		Tobin’s Q	.011*	.026*	.144
25		ROA	.034*	.042*	.452
26	Foreign group dominated firms and firms with no dominating groups	Board Structure& Process	.002*	.308	.088
27		Index of Auditor Independence	.010*	.076	.038*
28		Index of Related Party Transactions	.001*	.002*	.001*
29		Tobin’s Q	.000*	.002*	.010*
30		ROA	.002*	.000*	.003*

Note:* denotes significance at $p<0.05$ level.
Grouping Variable: Nature of dominant shareholder ownership

The above table compares, across company groups (taken two at a time) the three corporate governance variables and the two firm performance parameters over a three year period; the results confirmed significant differences in firm performance (Tobin’s Q and ROA) and two corporate governance parameters(board structure and process and index of related party transactions) tested across different years for paired comparison and found that in as many as 20 paired comparisons (out of the possible 30 paired comparisons) the test for significance gave consistent result for all the three years of the cross sectional study.

The finding that there is significant difference in two of the three key corporate governance parameters (board structure and process, index of related party transactions) across the four groups of companies is an important conclusion from this study. This points to the need for evolving customized corporate governance policies, specifically directed at company groups that have similar dominant shareholder(s), instead of implementing a ‘one size fits all’ corporate governance measures across all companies uniformly. Mandating a universal standard for corporate governance that could be applied, across the board, for all companies in India, is unlikely to give the desired results and would remain a futile exercise.

Likewise, the significant difference in performance (in respect of both- Tobin’s Q as well as ROA) across the four categories of firms, classified on the basis of the nature of the dominating shareholder, points to a possible link between the nature of the dominating shareholder and firm performance that needs to be explored in greater detail for a fuller understanding of the relationship between the nature of dominant shareholder, key corporate governance characteristics and firm performance in the Indian context.

As in most emerging economies, Indian Companies are linked in some way or another to an economic group or conglomerate that exercises tight control over the firm and, as the findings of our study indicate, this very important linkage seems to impact not only the corporate governance characteristics of the firms but also its performance.

VI. IMPLICATIONS FOR POLICY FORMULATION.

Effectiveness of corporate governance regulations depend on having a robust policy that is not based on either popular perceptions or on common position (arrived at on the basis of the negotiation of the divergent views of various interest groups who are affected by the regulatory changes) or by transplanting alien concepts that may have worked elsewhere but which may not be suited to Indian situations. An effective policy must be based on robust theory and, before roll out of policy, the prescriptions need to be empirically tested on actual conditions and their validity established.

Unfortunately in India, not only are the regulatory changes (in corporate governance) not rooted in sound theory but are based on borrowed Anglo Saxon concepts that have limited applicability in the Indian context.

Over the last two decades, significant steps have been taken by the regulatory authorities in India to enhance corporate governance measures in India; however, these developments have closely followed efforts in other jurisdictions such as the U.K. (the Cadbury Committee Report) and the U.S. (SOX). As pointed out by Varottil (2009) the measures adopted in India do not recognize the differences between the outsider systems of corporate governance (found in the U.S. and U.K.), from which concepts such as independent directors, audit committee and CEO/CFO certification have emerged, and the insider systems of corporate governance (found in India) into which they have been transplanted; unless these differences are factored in by the regulators, courts, industry and academia, there are likely be difficulties in implementation of the enhanced corporate governance measures and their assimilation within the Indian corporate ethos.

For instance, dominant shareholder(s), in Indian companies, by virtue of being able to muster a majority of shareholders present and voting on such resolution can not only control the appointment of every single director (including independent directors) and thereby determine the constitution of the entire board but also can influence the renewal of the term of directorship. Assuming that one of the purposes of the independent directors (in the new Companies Bill,2012) is to protect the interest of the minority shareholders from the actions of the controlling shareholders, such a purpose can hardly be achieved given the current matrix of director appointment, renewal and removal, Varrotil (2010),Sarkar (2009).

Research across different countries has shown that differing ownership characteristics of firms across the world have led to the creation of different governance structures and there is no "one size fits all" kind of governance structure that has universal applicability, La Porta, Lopez &

Shleifer(1988); Claessens and Fan (2003), Klapper and Love (2002), Berglof and Claessens (2004), Singh and Zammit (2006), Maher and Andersson (1999).

The current approach, of implementing common, across the board solutions (largely based on transplanted solutions that are in use in the Anglo Saxon world) to improve corporate governance in India, is not likely to be effective as it suffers from two infirmities. Firstly, the current solutions do not satisfactorily address the issues arising from the prevalence of dominant shareholder(s) in India and, secondly, they fail to take into account the inherent differences in firms with different category of dominant shareholder(s). Clearly, the prescriptive corporate governance code being implemented does not address the real corporate issues in India and will not deliver the desired results.

What India needs is a home grown system of corporate governance, evolved from within, and implemented through focused solutions which recognizes the differences in corporate governance characteristics across firms with different dominant shareholder(s).

Satisfactory solutions to the corporate governance questions (in India) can be provided only through a better understanding of the peculiarities of the Indian business environment, its legal and cultural traditions and social structure, all of which would have an influence on the effectiveness of its corporate governance system. While some broad directions are emerging, which point to the future direction for corporate governance reforms, there is a need for greater research in this area, particularly with reference to the role played by the dominant shareholders, as that would help in determining the right answers to the corporate governance issues in India.

Holistic studies, which recognize the key influence of the nature of the dominating shareholder in Indian firms, would help to develop a more robust theory for corporate governance and provide a better understanding of the underlying issues that affect corporate governance in India. This, in turn, would help in evolving a framework for reforms that is appropriate to the Indian situation and ethos.

Such corporate governance reforms would have much greater chance of success as compared to any ad hoc reform measures which do not have a robust understanding of the underlying basis.

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