CHAPTER – II
REVIEW OF LITERATURE
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2.1 Introduction

A thorough understanding of previous literature is crucial to identify the state of research and development in selected area of the study. The availability of enormous literature on corporate governance across the world helped to lay a strong foundation for present study and to derive the gap. It showed the way ahead. More than 200 studies, relating to corporate governance, were reviewed. This chapter presents reviews of those studies which directly relate to the research. It comprises of 12 books; for conceptual understanding, 35 journal articles, 9 dissertations & theses, 8 reports and working papers, 11 studies from other online sources; for understanding practical application of corporate governance. The studies relate to different facets of corporate governance and belong to different time periods. The research gap and research objectives of the study are derived from these literatures.

2.2 Classification of the review

Review of literature has been classified based on different dimensions of the study and further within each section they have been ordered chronologically.

Basis of classification:

2.2.1 Ownership, board of directors, CEO-Chairman role duality and other internal mechanisms of corporate governance

2.2.2 Regulatory standards, CG practices, firm performance, and other dimensions

2.2.3 Pharmaceutical industry

2.2.1 Ownership, board of directors, CEO-Chairman role duality and other internal mechanisms of corporate governance

This section of literature review covers discussion on studies of ownership pattern, board of directors, board sub-committees, CEO-Chairman role duality, and other relevant dimensions of corporate governance. While some studies concentrated entirely on individual dimensions, some have touched upon these governance aspects jointly. And some have studied the effect of this on performance. For this reason we have provided a discussion on all above mentioned dimensions under single head.
L.A.A. Van Den Berghe and Steven Carchon (2001)\textsuperscript{4} intended to find out the difference in governance practices between family and non-family businesses and also within the group of family based on family ownership structure and generation. The study explored the relationship between ownership structure, board and management practices. The data for the study collected through an instrument from 2602 companies drawn from population of Belgium companies.

Bryan W. Husted and Carlos Serrano (2001)\textsuperscript{5} analyzed governance structure, industrial policy, ownership and control pattern and industrial relations, their changes and impact of such changes on the country’s development. This study found that, around 179 companies, trading in the Mexican stock exchange, are in reality controlled by families and publicly traded stock commonly represents only a small percentage of public ownership and also less holding of corporate ownership from institutional investors. 95% of family owned firms have a family member as CEO, which reduces agency problems between major shareholders and management, but leaves the problem with respect to minority shareholders. Interlocking directorates, cross-holding of shares, less participation of workers in the management of firms are the other attributes of Mexican companies. However, presence of minimum outside directors, CEO-chairman role separation, and strategic function of the board are few examples of changes in corporate governance that started in late seventies in Mexico. The reliance on foreign and institutional capital gave an impetus to some changes in corporate governance. But authors foresee the continuation of family control in foreseeable future.

James R. Booth et al. (2002)\textsuperscript{6} examined the existence of trade-off between alternative monitoring mechanisms. They argued that, the existence of one monitoring mechanism reduces the need for other alternative monitoring mechanisms. Alternative monitoring mechanisms include internal mechanisms such as outside directors, insider ownership and CEO or chairman duality and external mechanism such as regulation. It is evident in the study that one monitoring mechanism acts as substitute to other


mechanisms and found that there are tradeoffs in using monitoring mechanisms. Regulation indeed acts as a substitute for monitoring mechanism. To the extent that regulations reduce the impact of managerial decisions on shareholder wealth, effective monitoring by outside board members, inside director stock ownership, and CEO or Chair separation become less important in controlling agency conflicts.

The paper of Boniface Ahunwan (2002) investigates the prospects for economic reforms which contribute to more responsible governance and development. As the author states, corporate governance system in Nigerian firms started to be recognized during the post-colonial period. He studied the ownership structure which was found to be concentrated in Nigerian companies and there exist agency problems between management and shareholders, between majority shareholders and minority shareholders.

Study of corporate governance in Brazil by Flavio M. Rabelo and Flavio C. Vasconcelos (2002) shown that, ownership concentration is a fundamental characteristic of Brazilian corporate governance structure with state, local-family and affiliate multinationals being the major agents. The study reveals that, out of the sample selected, more than 50% of large and medium sized companies are managed by family and firms with pyramidal structure. The authors opined that, the concentrated ownership structure has raised the agency problems between controlling and minority shareholders. They argue that improvement of legal and institutional investor activism through the government interventionism would be a vital move towards the creation of an efficient corporate governance structure.

The work of Manohar Singh and Wallace N. Davidson (2003) is an extension of the work of Ang et al.’s (1999) on relationship between ownership structure and agency costs in small businesses. However, the authors took large public companies unlike small businesses taken by Ang et al. The variables studied are ownership structure (managerial ownership and outside block ownership), agency costs represented by asset utilization (the ratio of total sales to total assets), and operating expenses (ratio of operating expenses to total sales). Board size and

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composition are control variables. Authors find that higher inside ownership aligns managerial and shareholder interests and lowers the agency costs in terms of asset utilization and found insignificant relation when agency cost defined in terms of operating expenses. There exists insignificant relationship between outside block ownership and agency costs. It is found that board size is negatively related to asset turnover, but unrelated to discretionary expenditures. They suggest considering board composition, committee structure, and firm age and their impact on relationship between board and agency costs in future researches.

Sandra C. Vera-Munoz (2005) developed hypotheses to test the relationship between ownership concentration of controlling shareholders, the proportion of controlling shareholders on the board, the proportion of outside directors on the board, the proportion of outside supervisors on the supervisory board and the firms' performance. As per the findings; the ownership concentration has the most significant governance effect and has impacted negatively on firm performance. Furthermore, the governance role of the board of directors and supervisory boards is found to have been hindered by ownership concentration. The author concludes by saying that audit committee plays the role of ultimate monitor of financial reporting process and hence it must be vigilant, well informed, independent and overseer of the financial reporting process.

Lalitha S. Som (2006) asserted that at the firm level, the most striking and commonly agreed failures of CG practices in India have been widely perceived to be (a) ownership structure in companies, (b) failure of boards, (c) accounting practices, and transparency. Ownership concentration, prevalence of insiders and principal promoter, lack of protection for minority shareholders, lack of strict enforcement rights of regulatory authorities, disregard for disclosure norms and transparency are some of the endemic features of Indian companies have restricted Indian corporate sector's progress.

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Adam Angyal and Julia Csanda (2006)\textsuperscript{12} wanted to know the corporate governance structures in the Hungarian financial sector and to evaluate the casual relationship between corporate governance and outstanding financial performance of this sector. They choose financial sector due to its fame as one of the most profitable sectors in the country which had suffered painful consolidation period during nineties. Hungary is the first central European country to take up reform measures in the banking sector. During nineties, government embarked on the privatization of state owned banks in the country. This caused a change in the ownership structure of the banks and also insurance companies. The study uses the questionnaire developed by the University of Chemnitz. The questionnaire was modified to suit to the corporate structure of the country and that included five sections viz. general questions, section on ownership, section on top management, section on supervisory board, section on executive board and section on stakeholders. The sample includes 11 credit institutions and 7 insurance companies. However, the response rate is 40%. It is found that, 4 of the seven credit institutions are owned by foreign institutions and 3 institutions did not know about the official corporate governance codes issued by the Budapest Stock Exchange. And they found that corporate governance was not preoccupied in the Hungarian financial sector and the outstanding financial performance is not the result of outstanding corporate governance.

Yves Bozec and Richard Bozec (2007)\textsuperscript{13} analyzed the relationship between ownership concentration and the corporate governance practices of a group of 244 Canadian companies listed on the Toronto Stock Exchange. Overall empirical results showed a negative relation between the deviation from a one share-one vote rule and corporate governance best practices and a negative relation is found between ownership concentration and the board composition sub index.

Khaled Elsayed (2007)\textsuperscript{14} - The study explored to what extent CEO duality can affect corporate performance. Author concludes his paper based on his findings that CEO and chairmanship role separation and its positive association with firm performance vary with the corporate characters and/or industry context. Both CEO


duality and separation have associated costs and benefits. Hence, as they commence their exploration of corporate governance issues, Egyptian firms need to recognize that the structure of the firm and industrial activity are the main determinants that can boost the impact of board leadership structure on firm performance.

_Yabei Hu and Shigemi Izumida (2008)_\(^\text{15}\) stated that Japan is a developed country with typically concentrated ownership of firms in the hands strategically oriented stable owners, who concentrate more on the stable development of the companies rather than on equity return and control rights of the firm. They undertook the study on Japanese companies listed in Tokyo Stock Exchange between 1980 and 2005.

_Parmjit Kaur and Suveera Gill (2007-08)_\(^\text{16}\) stressed on the importance of ownership structure and control. Authors argued that legal and regulatory system in a country plays an important role in creating an effective corporate governance environment. This study attempted to find the relationship between ownership structure and other governance aspects such as board size and composition in 134 BSE 200 companies covering the period from 2000-01 to 2005-06. They found that ownership is concentrated in the hands of promoter shareholders and persons acting in their concert and management is primarily monitored by promoters. The results of the study emphasize the importance of distribution (ownership structure) and type of large shareholders. Authors opined that it is not only the distribution of ownership but also the types of large shareholders that have a significant impact on performance. They suggest companies to have small boards and trained independent directors on the board to increase its efficiency and effectiveness.

_Helen Wei Hu et al. (2010)_\(^\text{17}\) argued that in China’s publicly listed companies, like many other emerging economies, concentrated ownership is in existence. Ownership is concentrated in the hands of central and state governments directly and sometimes indirectly through state owned enterprises (SOE) and in the hands of domestic firms. The study found that, firm performance is negatively impacted by


ownership concentration and the governance roles of board of directors and supervisory boards have been hindered by the concentrated ownership.

**H.B. Kota, S. Tomar (2010)**\(^{18}\) examined the effects of corporate governance practices such as board size, CEO duality, ratio of non-executive directors and independent director acting as chairman of audit committee on firm performance. 106 Indian medium sized firms (Market capitalization), between 2005 and 2007 were studied to test the research hypotheses. It is found that, ratio of non-executive directors and independent director acting as chairman of the audit committee have no significant effect on firm performance. However, CEO duality and small boards contribute positively and significantly to the firm performance.

**Balasubramanian N. et al. (2010)**\(^{19}\) proposed to provide a detailed overview of the practices of publicly traded firms in India and to identify areas where governance practices are relatively strong or weak. It is found that- 1. 87% of the firms follow board independence rules under the Indian law, 2. Board chairman often represents controlling shareholders, 3. Related party transactions are in common practice, 4. 99% of the firms comply with audit committee requirements, but there is less uniformity in their operations, 5. Only 70% of the firms reported that shareholders approve all directors pay, even though it is a legal requirement, 6. Only 73% firms allow postal ballots, 7. Given that most firms have a controlling shareholder, the fraction of shares voted at the most recent annual shareholder meeting is surprisingly small, at a mean of only 58%. This suggests that minority shareholders often do not vote.

**Qaiser Rafique Yasser (2011)**\(^{20}\) argued that family owned firms constitute a major share in total number of registered companies around the globe. The ratio of family owned business ranges from 75% in UK to more than 95% in India, Latin America and Middle East countries. As most of the Pakistani companies are managed by families, researcher tried to know whether family controlled firms perform better than non-family controlled firms in Pakistan in view of corporate governance mechanism. The size of the sample is 134 companies listed in Karachi Stock

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Exchange and data gathered for a period of six years from 2003 to 2008. Family controlled firm is defined as; a. Founder is the CEO or successor is related by blood or marriage, b. At least two family members in the management and c. Family directors have managerial ownership (direct and indirect shareholdings) of minimum 20 percent in the firm. And leadership meant separate or duality leadership structure. It is found that there are significant differences between family and non-family controlled firms' performance when measured by Tobin Q, return on asset and operating cash flow. Variable wise analysis shows that, family controlled firms perform better than non-family controlled firms as regards Tobin’s Q. Contrast to this it is found that, non-family controlled firms are better at managing cash flows with mean value (0.062) higher than mean value for family controlled firms. Non-family controlled firms prefer to have more independent professional directors than their counterparts. There found no difference in leadership structure between family and non-family controlled firms. However, study found negative relationship between dual leadership and firm performance, which implies that separate leadership enhances the firm performance. Author suggests the regulators to take note of the differences in the practices of family and non-family controlled firms as most of family controlled firms do not comply with Securities and Exchange Commission of Pakistan’s guidelines.

Akhalumeh Paul et al. (2011) examined the relationship between the proportion of non-executive, outside directors in the board and the financial performance of Nigerian firms. Results show that outside non-executive directors do not create any economic value added though they may have some benefits.

Marc Van Essen, J. Hans Van Oosterhout Michael carney (2012) analyzed 86 studies carried out in 9 Asian countries with the aim of studying board attributes and firm’s financial performance. Authors, for this purpose, developed hypotheses regarding a) the relationship between board independence, size and CEO duality and firm performance b) type of ownership (family, institutional and foreign) and its impact on board independence, CEO duality and size of the board c) board attributes on R and D investment. And found that, there is no direct relationship between board

attributes and performance of Asian firms but, pointed at role of board as a concrete mechanism through which board attributes do indirectly affect performance. It also reveals that family ownership has a negative effect on board independence and board size and positive effect on CEO duality. It is observed that R and D intensity is positively influenced by dual board leadership structure in Asian firms which in turn leads to good financial performance of the companies.

**Darline Augustine (2012)**- The **dissertation** examined variance in firm performance in the microfinance industry. It focuses primarily on financial performance and to a lesser extent, social performance is also examined. Both quantitative and qualitative evidence suggest that organizational transparency as a proxy for good practice in corporate governance in the microfinance industry has positive implications for firm performance, irrespective of ownership or institutional environment. Findings of the study- a. Shareholding among family businesses is different from the shareholding pattern of non-family businesses where in investment companies, other employees, industrial partners and mother or holding companies are major shareholders.b. 70% of family owned firms have the same person as president of the board and CEO of the firm, however, there is no significant difference between family and non-family businesses with respect to appointment of independent directors on the board, c. The research confirms that succession is typically a problematic issue. Only 30% of the family businesses survive the transition to the second generation and 10% to the third generation.

The objective of study by **Arifur Khan et al. (2013)** was to investigate the influence of corporate governance practices on corporate governance disclosures in an emerging Asian country like Bangladesh. Authors concluded that, corporate governance structure, in particular internal governance structure, is likely to play a vital role to reduce legitimacy gap through environmental and social disclosures. The overall findings of the study suggest that, internal corporate governance practices such as managerial ownership or public ownership, board of directors, presence of audit committee and CEO duality are vital in determining the extent of corporate social

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responsibility disclosures. While managerial ownership has negative impact on CRS disclosures, public and foreign ownership have positive impact on CSR disclosures. Likewise, the independent board and presence of audit committee have positively affected CSR disclosure practices. However, CEO and chairman role duality do not show any significant effect on CSR disclosure standards. Further authors suggest for a revision of governance model in companies, requiring the infusion of more independent directors on the board and prohibiting a family member to act as CEO.

Apostolos Gotsias and James G. Tompkins (2013) 25 - A corporate Governance game was designed for graduate or undergraduate students to discover the conflicts of interests existing among shareholders, board of directors, management, and auditors. Following three significant conflicts of interests were identified; conflict of interests between management and shareholders, conflict of interests between board of directors and shareholders and conflict of interests between auditors and shareholders. Role playing exercise was used to bring out the possible solutions for the problems. The solutions so derived were then compared with the existing corporate governance regulations in United States.

M. Subramanyam (2013) 26 - The overall objective of the study is to review and evaluate the corporate governance disclosure practices of selected listed Information Technology companies in India. Researcher takes a sample of six companies which are top in terms of exports and the study spans for a period of eight years from 2004-05 to 2011-12. The study encompasses disclosure about boards, audit committee, remuneration committee, shareholders grievance committee, and risk management committees which are analyzed for individual companies. Sample companies have maintained 50% non-executive directors in the board over the period of the study. There found irregular attendance of chairman in annual general meetings. No information disclosure about literacy and expertise of audit committee members was observed. It is observed that companies disclose only the number of shareholders complaints received, but they are reluctant to disclose the details of the complaints received. And only 25% of the samples have separated the roles of CEO

26 Subramanyam, M (2013). Corporate governance and disclosure practices in listed companies- A study of select IT companies in India (Doctoral thesis). Sri Venkateswara University, Tirupati, India.
and chairman of the board. The study has a small sample and corporate governance disclosures considered are also not wide.

2.2.2 Regulatory standards, CG practices, firm performance and other dimensions:

‘There are two approaches in driving the implementation of good corporate governance (GCG), ethics-based approach, and regulatory-based approach’ (Mas Achmad Daniri, Chairman, National Committee on Governance, 2006)\(^{27}\). Ethics-based approach does not require compulsion on compliance with rules and regulations. The actions of business practitioners result from their ethical conscience. On the other hand, regulatory-based approach lay down a set of rules which need to be followed by these businesses. Their ethical instincts go together with established standards of business conduct. We see countries having their own rule of the land for the betterment of corporate governance in listed public companies. Stock exchanges are at the top in the list of monitors of listed companies. Their regulations are generally enforced through listing agreements. Apart from stock exchanges, Government bodies, Non-governmental Organizations, and academic institutions set corporate governance codes that lead to efficient governance system in corporations. We find a large number of studies on level of compliance with such standard codes of corporate governance. Moreover, the effect of CG in improving the firm performance (financial and others) has motivated many academicians and researchers to study the relationship between the two. Thus we devote this section for studies on enforcement and compliance with corporate governance practices and their regulatory aspects in India as well as in various other countries and relationship between CG practices and firm performance. And also on other dimensions which do not fall into above classifications, but still relevant for the study.

Bernard Black (2001)\(^{28}\) - according to the author corporate governance behavior includes the governance rules adopted by the firms and the behavior of insiders in the firm. Author strongly opined that in a country like United States, governance laws are accepted and largely adopted. Therefore, it becomes difficult to


estimate the differences in relationship between firm performance and corporate governance due to little variations in the governance behavior among US firms. Thus, countries with weak governance laws provide a suitable context to test the governance behavior and firm’s market value. So, study advocates Russian firms give a suitable test case because of weak enforcement of governance and securities laws, self-dealing behavior of insiders and absence of reputational risks. Sixteen large Russian public companies considered as sample for the study. Author used ‘fall 1999 corporate governance rankings’ developed by an investment bank Brunswick Warburg. The governance rankings were combined with ‘actual September 1999 estimates of market capitalizations’ for these firms by another investment bank Troika Dialog. The fall 1999 corporate governance rankings assign ranks on 0-60 scale. Higher weights represent higher risk and therefore high ranking represents worse governance. The actual September 1999 value ratios of potential western market capitalization use firms’ actual market capitalization in Russian stock market to potential western market capitalization if the firms were operated in western market. Simple regression method was adopted to estimate the relationship between corporate governance rankings and value ratio (ratio of actual market capitalization to potential western market capitalization). The study found a statistically significant relationship between these two variables. It is important to note the finding that one-standard-deviation improvement in governance can cause eight-fold increase in firm’s value.

Ananya Mukherji Reed (2002) asserted that India like many other developing countries has been moving towards the adoption of an Anglo-American model of corporate governance in recent years due to the combination of global political-economic pressure and problems arising out of the previous business house model of governance. Basically, author attempted to answer two questions in the study. First, why Anglo-American model of governance has been adopted? And secondly, can it be justified? The first question has been addressed through the analysis of historic models that were existent in India viz., managing agency model in colonial period and business house model which was in effect from 1956 to 1991. Some governance flaws (such as, control by managing agencies, interlocking and inter-corporate investments, etc.) associated with these models and economic reforms

in early 1990’s drove Indian companies towards the adoption of Anglo-American model of corporate governance. The second question has been addressed taking into consideration the claims made in favor of Anglo-American model. They are corporate growth, increased shareholder activism, and employment generation. But, it is found that, there are no much changes in the structure of corporate governance between business house and Anglo-Saxon models of governance with respect to the mechanisms of control like interlocking directorates, etc. The results, as found by the author, were not promising.

**Diane K Denis and John J McConnell (2003)**

surveyed two generations of research on corporate governance around the world. These studies examined individual governance mechanisms particularly board composition and equity ownership in individual countries. The second generation of international corporate governance research considers the possible impact of varied legal systems on the structure and effectiveness of corporate governance and compares systems across countries.

**Tarun Khanna and Krishna G. Palepu (2004)**

analyzed the manner in which Infosys has attempted to shape corporate governance practices in India more generally, and why these attempts have had limited effects thus far. There is only limited diffusion of such practices to other firms in the software industry and to other industries in India. This study explores several reasons why, in practice, the effects of globalization on corporate governance convergence are somewhat limited.

**Vidhi Chhaochharia and Luc Laeven (2009)**

argued that many firms have adopted such governance attributes beyond what can be considered the norm in the country, and such improvements in corporate governance are reflected in higher market valuations. Firms that do not adopt sound governance mechanisms tend to have concentrated ownership and sizeable free cash flow, consistent with agency theories based on self-interested managers and controlling shareholders.

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Kenneth MacAulay et al. (2009) investigated the effects of new Canadian corporate governance rules, 2005 in ‘comply or explain’ regime. They believe that companies explanations based on comply or explain regime enables the investors to decide whether to sell or hold the companies securities. The study is concentrated on Canadian firms. The Canadian firms are relatively small in size and are closely held firms unlike the US firms which are large and are widely held. Authors opined that the comply or explain rule give firms with flexibility as to choose the standard based on the cost and benefits involved in complying with said standard and which increases firms performance. Hence, principle-based regulation system is preferred (comply or explain which is voluntary) to rule-based system (mandatory) that exist in US. The study, thus, examined the changes after the implementation of National Policy 58-201 on Corporate Governance Guideline and National Instrument 58-101 on Disclosure of Corporate Governance Practices in 2005 and the impact of changes on the relationship between corporate governance and firm performance. Authors criticized the use of global Corporate Governance Index which excludes small firms and they develop a broad index based on the new guidelines with inclusion of small firms also which form a major part of Canadian market. The sample companies include all Toronto Stock Exchange listed companies except those in the financial and insurance sectors. The data gathered from annual reports, proxy statements, and management information circulars of sample companies for period 2003 to 2007. Periods of the study are so categorized that, years 2003 and 2004 represent the period before the implementation of the new regime, year 2005 is the year of implementation and years 2006 and 2007 are period of post implementation.

They found governance scores having an increasing trend from 2003 to 2007. And it is interesting to note that although the increase in scoring is small for large companies, corporate governance scores increase with size and majority of small firms with poor governance score are vanished from the Toronto Stock Exchange. The positive relationship between corporate governance and firm performance is disappeared 2005 onwards, possibly because of the reduced ability of firms to signal differences amongst themselves by their corporate governance practices. It may also
reduce the ability of firms to choose their optimal set of corporate governance practices.

Victor Zitian Chen et al. (2010)\textsuperscript{34} found supportive evidence for their argument that controlling shareholders’ expropriation cannot be mitigated through good governance practices (viz. active board, separation of Chairman and CEO, presence of outside directors in board and two-tier board) in an emerging economy like China. Because, most of the governance practices which are considered to be good, are designed to resolve the conflicts between shareholders and management and between controlling and minority shareholders. In addition, directors in those countries are not fully independent of controlling shareholders and the role of supervisory board is very weak.

Basak Denizci Guillet and Anna S. Mattila (2010)\textsuperscript{35} studied the nature and extent of corporate governance provisions in the hospitality industry in United States. The industry has been divided into three segments for study purpose viz. hotels, restaurants and casinos. The data were collected from sources such as Center for Research in Stock Prices (CRSP), RiskMetrics and Standard and Poor’s Compustat database and covers a period of eight years. Authors considered 28 corporate governance variables listed in RiskMetrics, which were grouped into five subcategories a. Delay- anti takeover defenses, b. Voting- shareholders voting rights, c. Protection- executives protection against job related liabilities or compensation in the event of termination, d. State- State laws and e. Others. Gompers et al. G index was also adopted which explains Firms with the G index value of less than 9 are placed in ‘firms with stronger shareholder rights’ portfolio. Firms with the G index value of more than 10 are placed in ‘firms with weaker shareholder rights’, portfolio. The analysis was carried in two parts. First part analyzed the differences between five subcategories of governance provisions. The second part analyzed the relationship between G index and performance measures. Performance variables include market value, ROA, ROE, profit margin, leverage, capital expenditure per asset and Tobin’Q. The study shows that, the industry level G index is relatively stable in all the years, except 1995 where in the hotel segment has higher G index followed by restaurant


and casino segments. The G index is high at 8.90 to 9.98 indicating relatively weaker shareholder rights in the industry. As each provision in the G index represents restrictions shareholders rights decreases with increase in governance index. Further the results indicate that hospitality firms with weaker shareholder rights tend to be relatively larger in size, have relatively higher earnings per share, closing stock prices, return on equity, lower capital expenditure per assets and higher leverage ratios.

**Reema Sharma (2010)**36- The objectives of the study were to evaluate the corporate governance disclosure practices as per clause 49 of the listing agreement and their impact on firms’ financial performance through case study of some award winning companies in power, iron & steel, sugar, pharmaceutical, cement, textile, paper, automobile and software sectors. Sample of the study includes 112 companies listed in India. The study period was from year 2001, the year in which clause 49 of the listing agreement was implemented, to 2005. But, out of 112 companies, only 61 % of the sampled companies started following the code from the very first year of its implementation. However, no significant association has been observed between corporate governance and financial performance in these companies. It is found that compliance level regarding few items on clause 49 of the listing agreement is not 100 %. Software industry, among other industries taken for the study, scores more. It is also found that, companies have not adopted the whistle blower policy till 2003-04. However, in the year 2004-05, 7.14% of the sampled companies have adopted this mechanism. Only 2.63% of the sampled companies on an average have disclosed the code of conduct for its directors and senior management personnel. Infosys is the only company which has disclosed CEO and CFO certification of financial performance. And it is also found that corporate governance has positive impact on return on asset in drug, pharmaceutical and software industries. She concludes that managers must try to implement governance code with true spirit. And as respondents see board of directors and audit committee as important aspect of governance, companies should give more care in the constitution of board of directors and audit committee. She also suggested taking up ownership variable and inter-industry comparison for future research.

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Yarlagadda Venkata Ramana (2011) conducted a study with the objectives of investigating mandatory disclosures in corporate governance and to analyze corporate performance and governance in selected industries in India. The study was conducted on a sample of 170 BSE-500 companies taken from 8 sectors viz., Agriculture, Capital Goods, Chemical and Petrochemical, Finance, Information Technology, Metal, Metal Products & Mining, Gas & Oil and Transport Equipments. Period of study is from 2001-02 to 2005-06. Corporate governance practices such as BOD, audit and remuneration committees etc. were taken as independent variables, and the impact of these on firms’ performance was analyzed. They have studied the relationship between the variables in each sector. And found positive relationship between BOD and firms’ performance in finance, oil & gas and transport sectors. Audit committee’s role found to be insignificant in all the sectors except in chemicals & petrochemicals sector where the concept of ‘Audit committee performance measurement’ is still in beginning stage. Negative association between risk management committee and firm performance was found in finance and found total absence of disclosure about the committee in chemical & petrochemical, metal and mining sectors. There found a negative influence of remuneration committee on performance in metal, metal products & mining, oil & gas sectors and its inadequate role in rest of the sectors. The existence and disclosure regarding shareholder or investor grievance committee has a positive impact on firm’s performance in agriculture sector whereas, capital goods, metals & metal products & mining and transport equipments sectors have experienced negative impact of this committee on firms performance. There is a need for compliance with adoption of non-mandatory provisions and found insignificant relationship between non-mandatory disclosures such as special remuneration packages, directors training, unethical practices reporting mechanism etc., and performance found in agriculture, finance, chemical & petrochemical, information technology, oil & gas and transport equipments found because of inadequate contribution of the companies towards these disclosures.

Further, there found a need for more board meetings and more board members participation. Researcher states that, short tenure and vacant positions cause ineffectiveness of the board. The postal ballot mechanism found to be ineffective.

Related party transactions disclosure and penalties paid for non-compliance with capital market issues have negative impact on financial performance. The researcher suggests companies to go beyond and adopt governance measures in order to improve transparency in the governance.

*M. D. Saibaba (2011)*[^38] opined that corporate governance is affected by the size and sector of the firm and listing on foreign bourses. Researcher developed an index based on 21 parameters which were uniform across all sectors and found consistently in the annual reports. All 21 parameters were broadly grouped under four indices such as board structure index, auditing system index, investor management and disclosure index and external control mechanisms index. The study is concentrated on BSE 100 companies for a period of five years from 2004 to 2008. And the number of companies each year varied due to non-availability of annual reports. Each parameter assigned 1 for positive response and 0 for negative response. Apart from corporate governance index other variables like, assets log, sales, promoters’ holdings, and CEO duality were considered as independent variables. The financial parameters include Tobin’s Q, ratio of market value of shares to book value of shares and return on asset. Multiple regression model is used. Study revealed a positive and significant relationship between corporate governance index and financial performance. There found positive and significant effect of promoters’ holdings on financial performance as measured by Tobin’s Q and positive impact of board of directors on firm valuation. However, presence of independent directors on the board and separation of CEO and chairman roles have no influence on firm valuations. It is suggested for further investigations on the role of independent directors in India in the context of existence of large number of family owned companies. However, the study failed to measure the impact of other shareholders such as general public, mutual funds, insurance companies, FIIs etc. The present study considers the impact of these on financial performance of selected pharmaceutical firms.

*Lakshmana Rao A (2013)*[^39] - The first and foremost objective of the study is to know the extent of existence of corporate governance in India and its essential


elements. The other objectives are to examine how far the companies are implementing the methodologies of corporate governance, to examine how far the rating methodologies prescribed for apex bodies are possible to implement and to examine the level of transparency prevailed in Indian Corporate Entities in particular in Paper Industry. 12 paper industries were taken for the study. As observed, the state of corporate governance in paper industry is not up to the required level. Out of 12 companies selected, only 2 companies have a very good structure of corporate governance and 6 have scored average and rest were poor in adoption of good corporate governance practices. And the practice of measuring corporate governance in paper industry found to be in adequate by studying the system of corporate governance rating in the industry. It concludes that investors’ confidence in capital market can be protected through transparency and accountability. Transparency and accountability can be instilled among companies through better corporate governance procedures. Hence, regulators should develop an efficient governance framework and corporations ought to follow them for betterment of their governance.

Preethi M (2013)\(^{40}\) chose five nationalized banks namely Corporation Bank, Canara Bank, Punjab National Bank, Vijaya Bank and Syndicate Bank for analyzing the corporate governance disclosure level and its impact on banks performance. Researcher has also undertaken inter-bank comparison on aspects of board composition, board committees, board meetings, and disclosure level. Further, this work studied shareholders’ opinion on corporate governance practices in selected banks and whether their investment decision is determined by corporate governance. Study period covers years from 2005 to 2012. Study used a combination of secondary and primary data. A corporate governance index constructed based on the information derived from secondary sources such as clause 49, management discussion and analysis, directors’ report prepared according to Companies Act 1956, profit & loss account and balance sheet prepared according to Banking Regulation Act, 1949. And questionnaire consisting dichotomous questions was used to collect primary data from 150 shareholder respondents. Questionnaire contained 65 questions on mandatory, non-mandatory, and other requirements of corporate governance. Wherein, presence of disclosure carried one mark and absence of disclosure carried zero. The percentage

disclosure score for each bank was calculated by dividing actual disclosure score from maximum possible score to be obtained from the bank. Financial performance of banks was measured in terms of CAR (Capital Adequacy Ratio), ROA (Return on Asset), and NPA (Non-Performing Asset).

According to the findings of the study we can see the presence of code of governance, board of directors, audit committee and shareholders’ committee related aspects in the annual reports of all selected banks. There found least disclosure about postal ballot. All banks stood well in disclosure related to means of communication except disclosure on presentations made to institutional investors and outstanding ADRs, GDRs and convertible instruments. Study did found 100% disclosure of non-mandatory requirements and other requirements. Hence, it shows that 100% disclosure is seen only in very few dimensions of the study. The analysis of relation between corporate disclosure level and financial performance was done to each bank separately. It found that there exists a positive and significant relation between corporate governance and firm performance. The analysis of shareholders responses depict maximum number of shareholders belonging to the age group of 31-45, majority being men. 90.67% of them agree that they get all documents before shareholders meetings held. Majority of them agreed the complaints of minority shareholders are handled by banks. 45% of shareholders opined that their investment decisions are not affected by corporate governance practices of banks. Shareholders advocate adoption of effective monitoring of loan accounts and thereby reduce NPAs which negatively impacts the share value. It is concluded that there is need for one comprehensive law to bring in uniformity among banks in governance practices. Hence, regulators need to work on that and they also have to check compliance regularly to ensure proper compliance.

Akbar Riyasha (2013) took up the study with objectives to find out the significant relationship between corporate governance practices and firm performance and to suggest listed Sri Lankan companies to improve the performance efficiency by adopting best corporate governance practices. This study is conducted on 27 manufacturing companies listed in Colombo Stock Exchange covering data from 2007 to 2011. It is found that, there is no significant relationship between firm performance

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and corporate governance practices such as board leadership structure, committees and number of non-executive directors in the board. However, the researcher suggests systematic review of current corporate governance practices for reframing best corporate governance practices.

*Neelam Bhardwaj and Batani Raghavendra Rao (2014)*\(^{42}\) investigated corporate governance practices in Indian firms. They chose 50 CNX Nifty index companies which cover 22 sectors of the economy. The study period covers two years- 2010-11 and 2011-12. They use revised clause 49 of the listing agreement to benchmark the corporate governance practices of CNX Nifty 50 companies. The reporting practices of sample companies are rated and analyzed as those with disclosure and as per provision, those with disclosure but not as per provision and lastly as those with no disclosure. Authors found that, majority of the sample companies have followed and disclosed the information as per the requirement of clause 49. Very few companies have very good reporting practices beyond the requirements and follow the voluntary provisions also. Authors identify the need for extension of mandatory provisions. The study is restricted to CNX Nifty companies and gives scope for further research outside the CNX Nifty.

*Taruna & Arpit Shailesh (2015)*\(^{43}\) studied hundred companies belonging to ten different sectors such as automobiles, banks, FMCG, IT, oil & gas, pharmaceuticals, power, steel, telecommunication services and transport and logistics constitute the sample for the study. Data was collected from the annual reports of 2012-13 or 2013-14, considering mandatory and non-mandatory requirements of clause 49 of the listing agreement as standard. Companies were assigned scores out of hundred for governance practices and for this they use weightage method. Disclosure on company’s philosophy on corporate governance, board composition and board meetings, chairman and CEO duality, disclosure of tenure of directors, disclosure on definition of independent directors, separate meetings of independent directors and selection criteria of all directors including independent directors, board meeting follow-up system and compliance with board procedure, appointment of lead independent director, disclosure of other directorships or committee membership of


directors, disclosure of code of conduct, disclosure about board committees, disclosure & transparency, disclosure about general body meetings, disclosure of means of communication and general shareholder information, adoption of whistle blower policy, CEO/CFO certification, auditors certificate on compliance with corporate governance, disclosure of code of prevention of insider trading and disclosure of stakeholders interests are the factors covered in the study. A score card was developed and companies were grouped in five grades such as poor, average, good, very good, and excellent on the basis of these scores. While 19 percent of the companies have ‘excellent’ CG score, 44 percent companies ranked in ‘very good’ grade. 29 percent of the sample is grouped in ‘good’ category and only 8 percent of the companies got ‘average’ score. The study explored 100 percent adequate disclosure about directorship or committee membership or chairmanship of all directors. However, Only 35 companies have made appropriate disclosure about past board meeting follow up system and compliance with board procedure. Another finding is that 89 companies scored zero for not providing a post for lead independent director. About 96 percent companies do not publish audit committee report.

There found a satisfactory disclosure and compliance on matters of related party transaction disclosures, compliance with capital market matters, disclosure on accounting treatment and risk management, disclosure of director’s remuneration policy and management discussion and analysis, disclosure of shareholders rights and audit qualification. Almost all 100 sample companies have adequate disclosure about general body meetings. On the other hand, adoption of non-mandatory requirements such as training of board members and evaluation of non-executive directors could be found only in few companies. Sector wise analysis of corporate governance scores shows that, IT sector has highest mean (81) CG score with better governance over other sectors, followed by FMCG sector with mean score of 80.70. Power sector and oil & gas sectors stand next with a mean score of 79.40 and 78 respectively. Banking sector has a mean of 76.30, telecommunication sector- 75.60, steel sector -73.30, pharmaceuticals- 72.90 and transport & logistics - 71.40. And one way ANOVA analysis (0.097) shows that, there is no significant difference between governance practices followed across different sectors at 0.05 level of significance.
V.R. Sridhar and Dr. M. Sakthivel Murugan (2016)\textsuperscript{44} evaluated the factors influencing corporate governance practices and examined the relationship between corporate governance practices and financial performance of listed companies. They considered top 50 NSE and BSE listed companies from different sectors as sample and data were collected for the year 2013-14 and the financial performance variables were taken as the average of five years from 2009-10 to 2013-14. They categorized the governance practices as structure of the board, board’s process, board committees, investor grievances committee, transparency & disclosure, safety & health, CSR initiatives, risk management, internal control systems & adequacy, whistle blower mechanism and independent auditor’s report. The study found a significant relationship between corporate governance variables and financial performance of the organizations. They also found that majority of the sample companies are following best corporate governance practices and some of them having governance practices beyond the mandatory requirements of revised clause 49 of the listing agreement.

Qiao Liu and Zhou (Joe) Lu (2007)\textsuperscript{45} considered ‘tunneling activity’ to examine the relationship between earnings management and corporate governance in China’s listed companies. Authors state that China’s stock market has seen inherent links between earnings management and tunneling because most of the listed firms in China are spin-offs of large state owned enterprises. And these state owned enterprises hold, on an average, a controlling majority of 44 percent of shareholding. Further, in most of the cases the managers of listed firms are appointed by their parent companies. Thus China’s stock market is used by state owned enterprises as a vehicle to raise capital and improve operating performance. The ownership in these enterprises is concentrated in states as they want to keep more equity interest with them. The state’s involvement creates conflicts between controlling shareholders and minority shareholders. Generally local governments act as controlling shareholders. They appoint management of the companies and as a result management takes actions that benefit the controlling shareholders. Granting loans to controlling shareholders and a large number of related party transactions with controlling shareholders are common form of tunneling in China. It is evident from the study that earnings


management in China is pervasive because of various reasons. First, the condition for delisting the listed companies in China is based on accounting figures such as net income or ROE. Second, the companies’ right to issue right shares is also based on accounting profits of the companies which persuade the controlling shareholders to manipulate figures to maintain certain threshold. The other reasons being are high private benefits for controlling shareholders, poor level of corporate governance and weak protection of minority shareholders. Paper found that, the mean percentage of shareholding of largest shareholders is 44.11 % and the largest shareholders are states which exert control directly through state asset management companies or indirectly through their holding companies. Top executives hold a very little percentage of shares. However, it is found that about 12.43% of sample companies have combined the roles of chief executive officer and board chairman. On the whole, the study documents incentives to manage earnings and relate these incentives to controlling shareholders’ tunneling activities and finds that, the size of the private benefits to controlling shareholders are related to earnings management.

2.2.3 Pharmaceutical Industry

The studies on corporate governance in pharmaceutical industry are very less and they do not concentrate entirely on governance issues. In few available literatures only a small number of pharmaceutical companies are studied along with other sectors.

Carol A. Adams and Nongnooch Kuasirikun (2000) study the reporting on ethical issues in annual reports by large UK and German Chemical and Pharmaceutical companies. Authors collect data for a period of ten years from 1985 to 1995. Reporting on ethical issues, in this study include; environmental reporting, product marketing and pricing, product safety and testing, community involvement and public welfare, charitable donations and activities, political donations and activities, equal opportunities, and legal proceedings, litigation and liabilities. The sample consisted of all UK and German companies in the chosen industries falling within the top 400 companies in the Times 1000 in 1995. The data were collected using content analysis method from the corporate annual reports. This technique has

been widely used in determining the extent and nature of corporate social reporting. The analysis of the reporting on ethical issues show that, German companies have reached a matured level at the initial years of the study itself, while the UK companies shown an increased interest in reporting over the study period i.e, 1985 to 1995. The proportion of information on ethical issues is greater in German companies. There is more regulation in Germany requiring more reporting on environmental impacts in the annual reports. Authors say that the reason for lower reporting by UK companies, perhaps because of no legislation in UK.

**Nicola Lacetera (2001)** noticed a high degree of stability strategy and governance variables in each firm in US. Results of the study show that the ownership concentration and presence of scientists in the board has significant positive effect on research intensity, but presence of insiders in the board has no significant effect.

**Oxfam, Save the Children and VSO (2002)** are the developing agencies about health crisis in developing countries and this report is an attempt to study corporate social responsibility activities of pharmaceutical companies in developing countries. These agencies assert that being socially responsible does not only mean to be philanthropic in giving some charity and acting against social evils. Pharmaceutical companies should redefine CSR to include basic business issues like pricing, patent policies, research & development policies and etc. to address health problems in developing countries. It tried to look into the companies stand on drug pricing, patents regime, joint public- private initiatives, research & development and appropriate use of medicines as dimensions of CSR of pharmaceutical companies in developing countries. Eleven companies were selected for the study based either on their product portfolio or research and development facilities established.

In its response to the questionnaire sent out by Oxfam, Save the Children, and VSO, the pharmaceutical industry’s overall response, with some notable exceptions, lacked transparency and provided a poor indication of stakeholder accountability – both key considerations when assessing corporate responsibility. Firstly, the agencies proposed ‘tiered pricing’ as a necessary part of the solution to health problems. Secondly, the cost of patent protected drugs would be unaffordable by the developing

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countries. Thirdly, Oxfam, Save the Children, and VSO acknowledge the importance of working with a wide range of institutions to tackle pressing health issues in developing countries. They believe that joint public-private initiatives alone are always the most appropriate response of industry to these rich/poor diseases in developing countries. Lastly, companies have a responsibility to prevent harmful drug use by encouraging appropriate prescription and usage patterns in compliance with WHO guidelines. Ethical drug promotion, good clinical trial practice, and monitoring of adverse drug reactions are all core company responsibilities that cannot be waived by reference to weak and poorly-enforced national laws in developing countries or by the existence of industry guidelines. The report concludes by welcoming the companies’ interests in infectious diseases in developing countries. However, there is need for setting benchmarks on five areas of CSR (drug pricing, patents regime, joint public-private initiatives, research & development and appropriate use of medicines) as discussed above and disclosing the facts about meeting the targets to the public domain.

**Jagruti K. Dhadus (2015)** - The researcher has analyzed the corporate governance practices of top five pharmaceutical companies in India over a period of five years from 2006-07 to 2010-11. The objectives of the study include analysis of CG practices and processes, the determination of disclosure, accuracy, and timeliness of financial and non-financial information and to develop Corporate Governance Disclosure Index for Pharmaceutical companies. The methodology used in the study is inter-firm comparison of financial and non-financial disclosure practices. Each firm is compared with other company individually to get the disclosure score individually. This gives an opportunity to analyze each company’s position among the sample companies. Data has been extracted from annual reports, websites, Government circulars, periodicals, and journals.

Fourteen items from financial disclosure and fifty four items from non-financial disclosures are considered, where score 1 is assigned for disclosure of the item and score 0 for non-disclosure in annual reports. The results show that about 96.92% of the companies are in compliance with the financial disclosure and about 78.89% of companies are in compliance with non-financial disclosure. However,

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investment or performance in subsidiary companies is the major item with 31.42% being missing item in financial disclosure. Non-inclusion of letter from MD or CEO (80%), non-disclosure of vision or mission statement (74.28%), non-disclosure of chairman & CEO duality (94.28%), change in board structure (62.85%), non-disclosure of whistle blower policy (62.85%), functioning of the committee (60%), training of board members (60%), non-disclosure of employee stock option scheme (85.71), non-disclosure of postal ballot exercise or procedure (80%) and non-disclosure recognition for CG (97.14%) are major non-financial items that lack proper disclosure in selected companies. Thus, the study shows that the level of disclosure on non-financial items is relatively low than the disclosure on financial items. Researcher suggested that regulatory authorities should issue guidelines to individual companies regarding corporate governance and to revise applicable laws and codes from time to time to bring it to in line with global standards. The major limitation of the study is small sample size.

Ashwin A S (n.d.) asserts that while most of the firms in India are family owned there is also a significant shareholding by foreign, institutional, and public investors, banks, and financial institutions in India. Author studied 963 firm years’ data of 216 companies listed in the BSE between 2003 and 2009. He concludes the paper by stating that since the firms in India are predominantly family owned, the ability and motivation for these family owners to invest and successfully carry out innovative projects determine the overall level of innovation in the country and the focus (short or long term) on Research and Development innovations of institutional investors depends on how they look at such investments.

2.3 Conclusion

Above discussion about previous studies indicate that corporate governance has attracted extensive examination from the beginning of this century. Because, it was then the world witnessed massive corporate frauds and failures. Though corporate governance was not new till then, it saw tremendous reforms all over the world from then onwards. We can see studies from various economies along with a good number of studies in India too. They studied many governance practices individually as well as jointly. Some are cross-sectional studies of different industries. And a large number

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50 Ashwin A. S. (n.d.) Ownership structure and technology innovation: A study of Indian pharmaceutical industry. IIM, Bangalore, Karnataka, India.
of studies concentrate on the impact of corporate governance on firm performance. However, there is dearth of studies on pharmaceutical industry. Majority of the studies are descriptive in nature which evaluate the state of governance in sample firms. Few studies have embraced the legal aspects of law enactment and enforcement in other countries like China. One important observation is that, developing countries constitute a proper set up for the study of corporate governance.