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Ownership and Corporate Governance in Indian Firms

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1. Introduction

The nature of the corporate governance problems in corporations is largely dependent on their ownership and control structures, and the institutional set-up in which such corporations are embedded. At the same time, the ownership structure is one of the key internal governance mechanisms widely considered to mitigate governance problems both in widely-held firms and in those with concentrated ownership and control. The objective of this paper is to examine first the ownership structure of listed private sector Indian corporates as a source of potential governance problems,[1] and then to analyse how such problems can be alleviated by different ownership constituents. Additionally, based on existing empirical studies in the Indian context, the paper seeks to review the existing evidence on the link between ownership and corporate governance as manifested in firm performance. The importance of analysing the ownership structure of Indian corporates and its link to performance is underscored by the fact

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that the onus of several high profile corporate scandals both in India and abroad has been placed on underlying ownership and control structures.

The examination of the ownership structure of Indian listed private sector companies in this paper is based on relevant data available from the mandatory disclosure under Clause 35 of the Listing Agreement. Given the periodic changes in disclosure requirements with respect to major equity owners, the analysis of the ownership structure in this paper will be mostly based on comparable data available at a stretch since major changes were instituted in 2000–2001. Given that the ownership data prior to 2000–2001 was in a significantly different format than the data since 2000–2001, the data analysis will be primarily based on data post 2000–2001. Here also, depending on the comparability of the data, some analysis will focus on data up to 2005–2006, while some will extend to 2007–2008 (the latest year for which comprehensive ownership data is available at the time of writing). The analysis will be based on listed private sector companies in India, and both ownership and financial data will be sourced from Prowess, the computerised database on Indian companies published by the Centre for Monitoring Indian Economy (CMIE).

The rest of the paper is organised as follows. Section 2 briefly presents the theoretical background from an agency cost perspective of how the governance problem is manifested in ownership structures of corporations, on the one hand, and how ownership structures can serve as internal governance mechanisms to alleviate governance problems on the other. Section 3 discusses the characteristics of the ownership data with respect to listed Indian corporates. Section 4 analyses how agency problems in listed corporations are in-built in ownership structures specifically in the Indian context, while Section 5 focuses on how the important ownership constituents, namely promoters, banks and financial institutions, and institutional investors, play a role in the governance of corporates. This section also includes a review of the existing empirical literature examining the link between ownership structure and corporate governance with respect to Indian listed companies. Section 6 presents and examines select evidence with respect to minority shareholder expropriation in Indian listed companies. Section 7 concludes the paper.

2. Ownership and the problem of governance: Theoretical background

Ownership structure as a source of governance problem

While there are several alternative theoretical perspectives on the corporate governance problem that span across different disciplines, the dominant theoretical paradigm of corporate governance in economics and finance is the agency perspective, also known as the corporate finance perspective. Under this perspective, corporate governance deals with the ways in which the suppliers of finance to corporations exercise control and ensure accountability of company management in order to ensure they get the best possible return on their investment (Shleifer & Vishny, 1997). The foundations of this perspective can be traced back to the agency problem highlighted by Berle and Means (1932) in their pioneering work in the context of US corporations with dispersed share ownership, where shareholders (the principal) provide funds to managers (the agent) to put them to productive use and generate returns for the principal. Given such a separation of ownership and control, agency problems between the shareholders and managers can arise when due to either asymmetric information (managers being better informed about company performance and prospects) or unobservable efforts of the managers (moral hazard), the managers are able to take self-serving actions (such as appropriating funds for over consumption of perquisites, empire building) at the expense of the dispersed shareholders. Under such circumstances, Berle and Means (1932) raise the question of whether "social and legal pressures should be applied in an effort to insure corporate operation primarily in the interests of the 'owners' or whether such pressure shall be applied in the interests of some other or wider group" (p. 173). Corporate governance becomes meaningful in such a context, in terms of a set of mechanisms—both internal and external to the firm—that seeks to limit managerial discretion, or that provide incentives to help align the interests of managers with those of the shareholders. The relevance of such mechanisms from the corporate finance perspective lies in the fact that without such mechanisms, investors may be unwilling to provide low cost external financing to firms, the availability of which is critical for investment and growth.

While corporations with separation of ownership and control have dominated the US and the UK, cross-country studies have shown that there is a significant concentration of ownership both in developed countries (including the US and the UK) and in developing countries (La Porta et al., 1998). In Asian economies including India, concentrated ownership and control is the rule rather than the exception. Under concentrated ownership and control, the nature of the agency problem is essentially different from that present in diffuse ownership structures. While in the latter, agency problems arise on account of shareholder manager conflicts, dubbed in the literature as Type I or vertical agency problems, in the former, agency problems arise primarily due to conflicts between the two categories of principals—the controlling inside shareholders and dispersed minority outside shareholders, dubbed as Type II or horizontal agency problems (Roe, 2004). Type I agency problems are likely to be alleviated under concentrated ownership and control as the incentives of controlling shareholders to monitor management would be stronger on account of their substantial stakes in the corporation. This, however, does not preclude Type II agency problems, of the incentives of controlling shareholders from seeking to extract and optimise private benefits for themselves at the expense of the minority shareholders (Morck & Yeung, 2004). For instance, owners of business groups in regions such as Asia, Latin America, and Continental Europe, by virtue of owning substantial family ownership, are directly involved in the management of companies in which they have controlling blocks, including as a part of the board of directors. This can give them large discretionary powers over a firm's decisions which can be opportunistically used to expropriate minority investors.

Expropriation by controlling shareholders can be accomplished even under situations where shareholders do not have control through cash flow rights by using structural devices like dual class shares and stock pyramids that enable the creation of control rights far in excess of cash flow rights. For instance, in the case of family-owned business groups with a large number of affiliated firms, the controlling owner of one firm

can extend control over other companies in the group through the use of stock pyramids (Morck & Yeung, 2004). A pyramidal structure is one where a family firm A at the apex of the pyramid has majority ownership in a publicly traded firm B (say 51%), which has majority stakes in another publicly traded firm C (51%), which has majority ownership in a publicly traded firm D (51%), and so on. Given that A has majority control in B, and B has majority control in C, and C has majority control in D, A ends up controlling D, with as little as 13% equity. Thus through such pyramiding, the ultimate owner has successfully driven a wedge between control rights and cash flow rights, with control rights in D as well as other firms lower in the pyramid, far in excess of the cash flow rights. Such a wedge works as a vehicle for the expropriation of minority shareholders by controlling shareholders whereby the latter can—through various means at their disposal (like transfer pricing)—transfer wealth from firms in which cash flow rights are lower, to firms where controlling shareholders have higher cash flow rights (say from firm D to firm A).[2] This phenomenon known as tunnelling is one way in which the expropriation of minority shareholders can take place. Pyramid schemes are widespread in emerging economies. Faccio et al. (2001b) estimate that the 22 largest East Asian business groups controlled 31.2% of all listed corporations in their economies through pyramiding. Given the inherent tendency towards expropriation of minority shareholders by controlling shareholders in corporations with concentrated ownership and control, corporate governance in this context has involved the designing of a set of mechanisms, both internal and external to the firm, which would mitigate such expropriation.

Ownership structure as a mechanism of governance

The role of ownership as a mitigating mechanism for agency problems first came into sharp focus in the context of alleviating Type I agency costs in widely-held firms and the lack of monitoring incentives for diffuse shareholders in such firms. Two solutions to the monitoring problem in widely-held corporations have gained credence in the theoretical literature. The first one (referred to as the "alignment hypothesis" or the "convergence of interest hypothesis") is to offer concentrated ownership

stakes to the company management which would increase the overlap between ownership and control and help to align the interests of managers with those of the dispersed shareholders (Jensen & Meckling, 1976; Morck et al., 1988). The alignment hypothesis is less relevant in firms with concentrated ownership and control where higher shareholding by controlling insiders can automatically help to align their interests with those of outside minority shareholders by strengthening the link between the value of the firm and the wealth of the insiders. In fact, in countries with weak legal and institutional frameworks, concentrated ownership is seen as a panacea for Type I agency problems, and at the same time is viewed as a commitment device that sends signals to outside investors that the controlling insiders will not divert corporate assets or engage in other forms of expropriation (Gomes, 2000; La Porta et al., 1999). The second prescription to ensure efficient monitoring to reduce Type I agency costs focuses on the positive role that outside blockholders with relatively large equity positions can play in reducing agency costs. Known as the "efficient monitoring hypothesis" (Berle & Means, 1932; Pound, 1988), its basic premise is that large outside shareholders in widely-held corporations are likely to be efficient monitors as they have substantial investments at stake, and the voting power to ensure that the investments are not lost (Fama & Jensen, 1983; Jensen & Meckling, 1976), and can alleviate the free rider problem associated with small shareholders (Grossman & Hart, 1980), and are in a stronger position to use the proxy mechanism to discipline inefficient management (Dodd & Warner, 1983). Moreover, blockholders like investing institutions can engage in "relational investing," and the presence of blockholders like institutional investors can be socially beneficial as their interests tend to coincide with the interests of the society at large (Blair, 1995).

Concommitant with the benefits associated with large blockholdings in mitigating agency problems are the non-trivial costs as hypothesised under the entrenchment hypothesis, the conflict of interest hypothesis, and the strategic alignment hypothesis. Under the entrenchment hypothesis in the event of underperformance, insiders (by virtue of higher ownership

and control) can successfully insulate themselves from outside disciplining forces such as from the takeover market or the managerial labour market (Demsetz, 1983; Fama and Jensen, 1983; Stulz, 1988). Under the conflict of interest hypothesis, conflicts may arise between outside blockholders and minority shareholders due to the pursuit of objectives by the former that are at odds with those of the latter. For instance, blockholders such as institutional investors usually hold diversified portfolios and so reducing firm-specific risk through effective monitoring may not be their concern (Blair, 1995).[3] Finally, under the strategic alignment hypothesis, institutional investors who are outside blockholders, and managers who are insiders and often blockholders themselves, can find it mutually advantageous to cooperate and act against the interest of minority shareholders (Denis & McConnell, 2005). Strategic alignment between blockholders and management and mutual self-protection are possibilities particularly when a block-holding institution sells something—a product, debt or financial services—to the company in which it owns substantial stocks (Roe, 1994).

Several of the costs and benefits arising from the presence of large shareholders as highlighted in the studies of developed countries could be equally relevant in the context of developing countries like India. At the same time, some of the institutional specificities of developing countries—such as a less developed capital market, a less active takeover market, the absence of a well developed managerial market, the greater importance of implicit trust-based contracting, and a generic tendency towards insider control—could impact the costs and benefits of large shareholding in these countries in some unique ways, and so mechanically extrapolating the experiences of corporate governance systems in developed countries may not yield the necessary answers (Sarkar & Sarkar, 2000). Khanna and Palepu (2000) also argue that monitoring by large shareholders in developing countries may not be as effective as in developed countries because of the poor availability of information on the performance parameters of firms due to inadequate disclosure norms and weak enforcement, the presence of political connections which make disciplining difficult, and the opaqueness

associated with insider ownership arising due to pyramiding, cross-holdings, and association with a large number of privately-held firms.

3. Ownership structure of Indian firms: Data characteristics

Private sector firms in India can be broadly classified into domestic firms affiliated to business groups, domestic firms that are standalones, and foreign-owned firms. With respect to listed firms,[4] as of 2008, the Prowess database provides information for 1021 firms affiliated to Indian business groups, 2004 standalones, and 130 foreign-owned firms. While the number of standalones is higher, group affiliates have persistently dominated the Indian corporate sector both in terms of its share in total assets/sales, and in terms of market capitalisation. As of March 2008, listed group affiliates accounted for around 72% of the total assets of all listed firms, and only two of the top 20 listed non-financial companies are standalones; the rest are affiliated to business groups.

As is the case elsewhere, the ownership structure for any Indian corporate can be broken down into two major constituents—insiders and outsiders. The definition of insiders depends on the structure of ownership and control in a corporation—in widely held corporations, insiders are the professional managers entrusted with the day to day running of a company, and in corporates with concentrated ownership and control (such as family-owned corporations), insiders are the controlling shareholders. In the Indian context, as per the definition of different types of owners laid down in Clause 35 of the Listing Agreement, insiders are promoters and persons acting in concert (PACs),[5] whereas outside owners are essentially non-promoters who are further divided into institutional non-promoters and non-institutional non-promoters.

Since governance reforms gathered momentum in the late nineties, and with the recognition of the need to "upgrade and harmonise" disclosure standards at par with international best practices and to enable better price discovery in the secondary market (SMAC, 2004), the ownership disclosure requirements under Clause 35 have undergone important changes, one effective from March 2001, one from June 2006, and one

from February 2009. The first among these was the most fundamental, changing the disclosure requirements in three ways—re-categorising the major blockholders into two main groups, namely promoters (insiders) and non-promoters (outsiders); requiring the disclosure of the identity of all shareholders holding more than 1% equity along with their shareholding; and requiring the quarterly reporting of shareholder information instead of the existing annual reporting. Prior to 2001, insider holdings were distributed across several categories, such as under Directors and Relatives (as defined under the Companies Act, 1956), and were also clubbed under Corporate Bodies making it difficult for an outside observer to get an estimation of both the voting rights and the control rights of insiders. The reclassification into promoters and non-promoters in 2001 in the interest of transparency was done on the basis of subsections 11(e) and 11(h) of the Substantial Acquisition and Takeover Act of 1997 of SEBI (SAST, 1997) which defined promoters as persons or entities in *control*.[6] By adopting this definition, the regulations took into account for the first time the indirect control that promoters could exercise on a company by virtue of their holdings in other entities controlled by them, and such indirect control was clubbed under persons acting in concert (PACs). Subsequent to the first round of reforms in Clause 35, the definition of the type of equity owners (especially the term *promoters*) went through further refinements as it was being increasingly realised by regulators that the definition of promoters was "extremely critical for actions, regulations, research and analysis" (SMAC, 2004). Thus from April 2006, the definition of promoters and promoter groups, instead of being based on the SAST 1997, came to be drawn from Clause 40A of the Listing Agreement,[7] with the criteria for identifying promoters and promoter groups and their reporting becoming even more encompassing and detailed.[8] At the same time, the shareholdings of PACs which were separately disclosed between March 2001–2006 have come to be included under the purview of promoter groups.

With regard to non-promoter holdings, any shareholding other than promoters was required to be disclosed under the revised Clause 35 under the heading non-promoters which includes institutional non-promoters

and non-institutional non-promoters. In later revisions (after March 2006), the nomenclature has been changed to Public Shareholdings under which institutions and non-institutions are reported separately and in greater detail. Holdings by government-owned financial institutions, public and private sector commercial banks, government-owned and private sector insurance companies, public and privately-owned mutual funds, foreign institutional investors,[9] venture capital funds, foreign venture capital investors, central and state governments, and others, fall under institutional public shareholdings. Under non-institutional public shareholdings are corporate bodies, individuals,[10] and others.

In addition to the greater clarity in the definition of different ownership groups, the requirement to disclose the identity of all shareholders has created more transparency about the identity of the ultimate owners of a listed company, and has made it possible (to a considerable extent) to trace chains of control among group companies from the disclosed data. Here too the disclosure standards have changed over time towards greater transparency, changing from requiring the disclosure of the identity and shareholding of all owners holding at least 1% of outstanding equity (between 2001–2006), to requiring complete disclosure of the identity and shareholding of *all* entities under Promoter and Promoter Group irrespective of any cut-off level, and of all non-promoters with at least 1% equity holding (post April 2006).

It is important to mention in this context that the disclosure of data on insider promoter ownership based on the concept of control rather than on cash flows is rather unique in India when compared to disclosure practices in many other countries characterised by concentrated ownership. This is important because corporations with concentrated ownership are typically characterised by insiders having control rights in excess of cash flow rights due to pyramiding and cross-holdings, with control being achieved with cash flow rights as less as 20%. Hence the deduction of the extent of insider control based on cash flow figures (especially with respect to the ultimate owner) will underestimate the extent of such control. While Indian data completely discloses all entities that are in control of a particular

company, in many of the existing studies of concentrated ownership and firm performance in other countries, a large component of the analysis consists of the identification of shareholders (particularly insiders) who are in control using information available in the public domain to track down both their direct and indirect equity stakes through 'equity chains', and to define different thresholds in order to define control (see for example, Claessens et al., 2000; Lins, 2003, among others). Such an exercise may not be exhaustive due to the lack of data on all owners, as is recognised in Claessens et al. (2000).[11] In contrast, the mandatory disclosure of both direct and indirect ownership of all (at least 1% till 2006) of controlling owners including PACs, helps to largely eliminate the omission bias that is in-built in many studies.

4. Ownership structure and agency problems in Indian corporations

In light of the theoretical discussion in the earlier sections, this section examines the agency problems in Indian listed companies that could stem from their ownership and control structure. Specifically, the section focuses on two key aspects (from an agency perspective)—the prevalence of concentrated ownership and insider control, and the extent of complexity and opacity of ownership structures.

The prevalence of concentrated ownership and insider control

The Indian corporate sector is composed of both widely-held firms akin to those dominant in the US and the UK, as well as firms with concentrated ownership and control similar to those dominating most developing and emerging economies. Based on the definition of widely-held firms as firms where *no shareholder controls 20% votes*,[12] an examination of the ownership structure of 2075 private sector listed Indian firms as of March 2006, reveals that only a small minority of companies in the sample—7.2%—are widely-held, and the remaining firms (irrespective of their ownership affiliation) are characterised by concentrated ownership and insider control. The percentage of widely held firms in India is substantially lower not only with comparable estimates in countries such

as the UK, the US, and Japan which are dominated by such firms, but is also mostly lower than comparable estimates in countries in Europe and East Asia that are dominated by concentrated ownership structures.[13]

The pervasiveness of insider control in Indian firms is revealed in an examination of the ownership structure of 3155 domestic private sector listed firms in India using the shareholding data disclosed under Clause 35 as reported in Prowess for the financial year 2007–2008 (as shown in Table 1). Irrespective of the type of ownership affiliation, holdings by promoters constitute the single largest block (50.15%) for group affiliates, around 46% for standalones, and the highest (62.41%) for foreign firms. Further there are major differences in the constituents of promoter share across ownership groups, with corporate bodies accounting for the highest on average for group affiliates (32.90%), whereas individuals and family members accounted for the highest in the case of standalones (29.68%). In the case of foreign firms, foreign promoter share is predictably the largest constituent within the promoter group.

Table 1: Ownership structure (percentage share) of Indian corporates (2008)

	Group Affiliates	Standalones	Foreign	All
A. Promoter and Promoter Group	50.15	45.98	62.41	48.01
Individuals/ HUF	12.67	29.68	3.30	23.09
Government	0.17	0.06	0.08	0.09
Bodies corporate	32.90	13.31	5.01	19.31
Foreign promoters	3.54	1.94	53.77	4.59
B. Public Shareholdings				
Mutual funds	2.13	1.00	2.70	1.44
Banks and Financial Institutions	3.51	0.97	2.41	1.85
Foreign Institutional Investors	4.71	2.31	3.67	3.14
Corporate Bodies	9.78	11.51	5.09	10.69
Individuals	25.95	34.73	20.16	31.29
Others	3.17	3.11	2.99	3.13
Number of firms	**1021**	**2004**	**130**	**3155**

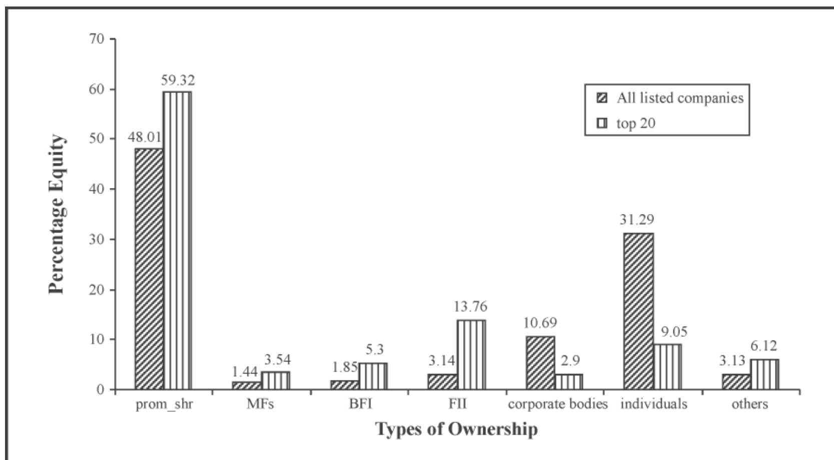
Notes: Constituents under A and B may not add up to A and B respectively due to rounding off errors. Similarly the sum of A and B may not add up to 100%.

Source: Author's calculations based on data obtained from CMIE Prowess database.

Considering outside shareholders, institutional holdings taken together are way lower than insider holdings, accounting for less than 10% on average, with the share of both mutual funds (MFs) and banks and financial institutions (BFIs) being less than 2%, and that for foreign institutional investors (FIIs) around 3% across all sample companies. With respect to non-institutional outside shareholding, holdings by private corporate bodies are around 10%, while holdings by individuals taken together are relatively important at an average of 31.29%, with the highest in the case of standalones and the lowest in the case of foreign companies.

Comparing the average ownership structure of the top 20 non-financial listed private sector companies in the sample ranked by market capitalisation as of March 2008 with the full sample of 3155 firms (Figure 1), we find that the concentration of promoter share on average is substantially higher for the top 20. Further, with respect to institutional ownership, the average holdings by MFs, BFIs, and particularly FIIs are markedly higher for the top 20 firms (as can be expected). Finally, the holdings of the top 20 firms, seventeen of which belong to family business groups, are much less dispersed as measured by the holdings of non-promoter individuals (9%) compared to the larger sample (31%).

Figure 1: Comparison of ownership structure of all listed companies and Top 20 listed companies (March 2008)



Notes: Total number of listed companies is 3155.

Source: Author's calculations based on data obtained from CMIE Prowess database.

Examining the extent and spread of insider control within business groups, an analysis of the distribution of promoter ownership is computed at the group level for the top 10 business groups ranked by total market capitalisation of the listed firms within a group. The relevant summary statistics presented in Table 2 show that on average, the promoter share within a group is substantially concentrated and higher than the average of the full sample in most cases. Even the values of minimum promoter holding in a group are at a higher level than the 20% cut-off that is necessary for gaining control. While there are substantially large differences in the size of group firms both within groups and across groups, the extent of insider ownership and control do not exhibit much difference.

Table 2: The extent of insider control in the top ten Indian business groups (2008)

Name of Business Group	Total Market Capitalisation (Rs. Crore)	Number of Listed Firms	Market Capitalisation (Rs. Crore)			Promoter Share (%)		
			Lowest	Mean	Highest	Lowest	Mean	Highest
Reliance Group	400875.9	4	1384.67	133625.3	329178.73	45.43	68.04	100
Anil Dhirubhai Ambani Group	255466.31	6	2828.23	42577.72	104914.49	35.95	59.67	89.91
Tata Group	237767.64	27	45.5	8806.21	79355.53	27.55	49.76	93.01
Aditya Birla Group	94057.8	8	42.79	13436.83	27078.33	25.19	48.31	70.4
Sterlite Industries Group	73902.52	5	41.1	18475.63	50565.25	38.8	57.96	80
Om Prakash Jindal Group	54220.52	7	126.82	7745.79	31906.95	43.29	52.38	62.3
Suzlon Group	39463.57	2	4.38	19731.78	39459.19	63.49	64.69	65.89
Mahindra and Mahindra Group	31389.68	9	15.03	3923.71	17095.03	22.62	52.52	83.57
Essar Ruia Group	30213.75	3	80.85	10071.25	23950.52	18.57	43.89	65.85
Jaiprakash Group	30032.91	3	832.35	10010.97	26546.7	44.54	60.88	74.78

Notes: Business groups with more than one listed firm as reported in Prowess were considered. Groups comprising only of financial firms were excluded from the list. The maximum stakes as reported are sourced from the Prowess database.

Source: Author's computations based on data obtained from CMIE Prowess database.

While cross-country comparisons are somewhat difficult given that the reporting of equity ownership data is not uniform, broad comparisons with other countries suggest that the Indian corporate governance system can by and large be characterised as a *hybrid* of the Anglo-Saxon 'outsider' system of the US and the UK (characterised by diversified equity ownership and less involvement of lending institutions), and the 'insider' systems of continental Europe and Japan (characterised by a

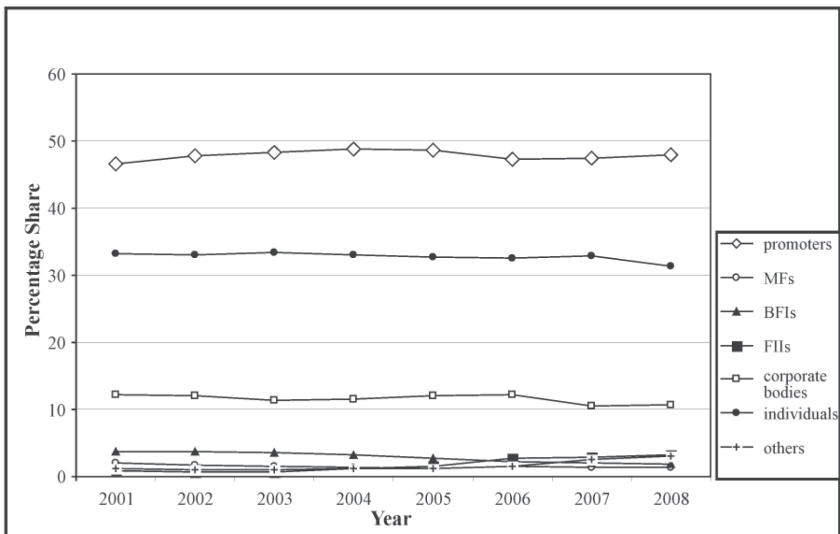
greater concentration of shareholder power residing with banks/families/ corporate bodies). Compared to other developing countries and the bank-based systems, India has a large number of listed companies—in fact the largest in the world—and while concentrated family ownership with its associated networks is the dominant ownership structure, the participation of the small investor in corporate equity in India is also not insignificant. Like the US and the UK, shareholder sovereignty is important in India. At the same time, equity holding by non-financial corporations in India (both as insiders and as outsiders)—a significant constituent of which is inter-corporate cross-holdings in group companies—is much higher than in the UK and the US and are more comparable to what is found in Germany and Japan.[14]

The prevalence of insider control in Indian companies and within business groups (as evident in Table 1) is in keeping with the persistence of concentrated ownership and control structures in India since the early years of Indian industrialisation in the colonial period and well into the post-independence period despite significant shifts in the institutional environment—from a regulated economy between the early fifties to the early nineties, to the increasingly liberalised environment since then (Khanna & Palepu, 2005; Sarkar, 2010). An examination of the evolution of concentrated ownership and insider control over a long duration in the context of India is constrained by the lack of comparable data mainly due to changing disclosure standards; the analysis of time trends can at best be limited to the period 2000–2001 to 2007–2008. This period is important nonetheless in view of the fact that several regulations since the nineties (such as those related to creeping acquisitions and share buy backs, changes in norms of entry for foreign institutional investors, as well as the partial privatisation of financial institutions) came into effect during this period and can be expected to lead to re-optimisation of equity portfolios in companies.

Two aspects of ownership trends are analysed, the first being the trends in the components of the aggregate ownership of an unbalanced panel of companies from Prowess for the period 2000–2001 to 2007–2008, and the second being the trend towards consolidation/divestment of insider and outsider ownership for a balanced panel of companies from Prowess during the period 2000–2001 to 2005-–2006. With regard to the first,

promoter ownership since 2001–2002 has consistently accounted for more than 46% of total equity, steadily increasing till 2003–2004, marginally dipping in 2004¬2005, and then touching the 48% mark in 2007–2008 (as indicated in Figure 2). Among institutional investors, BFIs remained the largest, although its equity stakes by and large declined over the eight year period, and by 2008 was almost half of its 2001 level. Like BFIs, the share of MFs too exhibited a declining trend, while FII ownership of Indian companies steadily increased, from being around less than 1% consistently during 2001–2003, to crossing the 3% mark in 2007–2008.

Figure 2: Trends in shareholding by major categories (2001-2008)



Source: Author's computations based on data obtained from CMIE Prowess database.

The second analysis of ownership trends examines whether there has been sustained consolidation or divestment of promoter ownership in some companies over time. Table 3 presents a balanced panel of 2120 companies between 2001–2006 (the set of companies by ownership groups in which promoter share ownership has increased, decreased, or remained unchanged over the period).[15] Additionally, taking all the interim years into consideration, the estimates are presented with regard to the set of companies that has undergone persistent *consolidation* (promoter share increasing continuously, from one year to the next, during the entire period), and the set that has undergone *persistent divestment* with a

consistently decreasing trend over the period. The key findings presented in Panel A and Panel B of Table 3 are highlighted in Box 1. While Panel A presents estimates of promoter consolidation/divestment, Panel B presents an analysis of the typical characteristics of firms in which promoters have increased/decreased their stakes during 2001–2006 in terms of market capitalisation (proxy for size), and promoter share, with the base year for comparison chosen as 2001.

Table 3: Trends and pattern of consolidation divestment of insider owners in Indian corporates (2001 and 2006)

A. Change in Promoter Share (prom_shr) between 2001 and 2006		
	Group Affiliates	**Standalones**	**All**
(1) Increase in prom_shr			
Number (%)of firms	421 (53.50)	594 (44.56)	1015 (47.88)
Median (mean) increase	4.87 (8.39)	6.01 (10.21)	5.70 (9.46)
(2) Decrease in prom_shr			
Number (%)of firms	318 (40.40)	568 (42.61)	886 (41.79
Median (mean) decrease	6.17 (10.13)	8.85 (13.06)	7.65 (12.01)
(3) No change in prom_shr			
Number (%) of firms	48 (6.10)	171 (12.83)	219 (10.33)
(4) Persistent Consolidation			
Number (%) of firms	28 (3.56)	34 (2.55)	62 (2.92)
(5) Persistent Divestment			
Number (%) of firms	16 (2.03)	22 (1.65)	38 (1.79)

B. Characteristics of Firms exhibiting change in prom_shr						
	Group Affiliates		**Standalones**		**All**	
	2001	2006	2001	2006	2001	2006
(1) Increase in prom_shr						
Median prom_shr	45.8	53.47	39.9	49.68	41.97	51.63
Median market cap	15.46	141.13	12.12	17.89	4.16	47.15
(2) Decrease in prom_shr						
Median prom_shr	53.17	45.65	52.79	39.5	53.1	41.76
Median market cap	18.08	140.01	3.12	15.65	5.23	37.54
(3) No change in prom_shr						
Median prom_shr	49.55	49.55	41.72	41.72	45.15	45.15
Median market cap	5.34	104.83	0.7	26.56	0.99	55
All firms in balanced panel						
Total number of firms	787	787	1333	1333	2120	2120
Median prom_shr	48.62	49.89	45.6	45.16	46.92	46.91
Median market cap	15.93	137.67	2.19	17.13	4.01	42.99
Mean market cap	330.51	1691.38	92.02	481.7	179.98	1027.93

Notes: Promoter share measured in percentage; market cap measured in Rs. Crore.

Source: Author's calculations based on data obtained from CMIE Prowess database.

Box 1: Trends in consolidation/divestment of promoter ownership (2001–06)

- Nearly half of sample firms (47.88%) have higher promoter share in 2006 as compared to their 2001 levels.
- A higher percentage of group affiliates have consolidated promoter share compared to standalones (53.50% and 44.56%, respectively) while the extent of consolidation is higher for standalones.
- Both the percentage of firms undergoing divestment as well as the average extent of divestment are lower for group affiliates (40.40% and 10.13%, respectively) as compared to standalones (42.61% and 13.06%, respectively).
- In the set of firms registering promoter consolidation, and those showing divestment, only a very small percentage have been achieved through 'persistent consolidation' or 'persistent divestment', (2.92% and 1.79% of the companies, respectively).
- In terms of size and promoter share, it is the median group-affiliate and the larger than median standalones with lower than average promoter share, that have consolidated.
- With regard to promoter divestment between 2001 and 2006, both group affiliates and standalones have in 2001 been on an average the larger than median firms in the sample with larger than median promoter ownership.
- Firms with no change in promoter share between 2001 and 2006 (although not ruling out off-setting changes in the interim years) are found to be on an average smaller than the median for the whole sample, and in the case of standalones, are among the bottom 25% of the sample.

The preceding analysis reveals that while both Type I and Type II problems are relevant in the Indian context, it is the latter type of agency problem that is of greater importance given the dominance and persistence of concentrated ownership and insider control in Indian corporates, both with respect to group affiliates and standalones. This is not surprising given that in emerging economies with relatively weak investor protection and rule of law, concentrated insider ownership is considered to endogenously evolve as an optimal response to mitigate Type I agency problems that affect widely-held corporations. In the case of India, while existing research shows that "laws in the books" both with respect to shareholder and investor rights are almost at par with international best practices, it the

rule of law, or "laws on the ground" that are weak (Sarkar & Sarkar, 2008). Thus shareholder monitoring costs in the case of separation of ownership and control in widely-held corporations are likely to be higher, which in turn explains the generic tendency towards maintaining concentrated insider control. The other key reason for the prevalence of concentrated ownership positions in Indian companies (including many of the largest companies) is that listed companies are highly leveraged with a relatively low equity base (on average). This allows insiders to control a significant portion of equity with relatively less investment.

Ownership complexity and opacity

While Type I agency problems are likely to be alleviated through concentrated ownership due to greater convergence of interests between inside and outside shareholders particularly in family dominated corporations in India where managers in most cases are *de facto* owners and the incentives to maximise the surplus is likely to be strong, this does not necessarily preclude the possibilities of expropriation of minority shareholders by insiders. As the Naresh Chandra Committee on Audit and Governance observed in the context of Indian companies (DCA, 2002), while a promoter who controls management and owns a majority stake is not expected to perform in a 'value-destroying manner,' the promoter (by virtue of being in control) can nevertheless act in a way that deprives minority shareholders their *de jure* ownership rights without necessarily affecting company profitability. As the theoretical discussion in Section 2 pointed out, the extent to which expropriation possibilities (i.e. Type II agency problems) are present largely depends on the complexity of ownership structures that arise from pyramiding, cross-holdings, and difficulties in tracking down the locus of ultimate control.

The historical perspective on ownership structures in India does testify to the presence of pyramidal ownership structures as well as cross-holdings in India from the very early years of business group formation (Hazari, 1966). That such structures are still prevalent is well documented in the existing literature (see for example, Bertrand et al., 2002; Masulis et al., 2009). Estimates based on 659 listed companies in India of which 189

are affiliated to 56 groups (Masulis et al., 2009) show that 10.02 per cent of the total sample of firms belong to a group and are controlled through a pyramid. Further, 4.10 per cent of market capitalisation of the sample firms is held by pyramid controlled firms.

One of the important aspects of the control structure of business groups that is evident from an analysis of control structures of other Indian business groups is that while family ownership is paramount, there is little *direct* ownership by family members. This is evident from the relatively low holdings by individuals in group affiliates but higher corporate holdings as compared to the overall average (as shown in Table 2), and largely reflects the fact that most business houses had developed as complex webs of companies and cross-shareholdings to take advantage of various government policies over the years.[16] This has left them with small, yet controlling stakes in group companies.

Apart from the complexity of ownership structure, an important source of agency costs in Indian listed companies that makes it difficult for an outsider to decipher the complete chain of ownership and control between firms is the *opacity* of ownership structure. Opacity is an important source of agency cost as it can help conceal the diversion and flow of expropriated funds. In the Indian context, one can identify three determinants of ownership opacity—the incomplete disclosure of the identity of owners, the fragmentation of insider ownership across a large number of owners, and the extent to which the ownership is in the hands of private entities. With regard to the first, between April 2002 and March 2006, disclosure regulations required listed firms in India to disclose the identity of only those equity holders *who have at least 1% share ownership*. Under such circumstances, ownership structure can be strategically engineered by controlling shareholders through the fragmentation of shareholding where individual ownership by insiders is deliberately kept at less than 1% to avoid mandatory disclosures. The larger the percentage of shareholding in the less than 1% cut-off and outside the public domain, the more opaque the ownership structure can be considered to be from the point of view of an outsider. This can be called Type I opacity. The second type of opacity

stems from the extent to which insider shareholding is 'fragmented' among its constituents; distributing a given shareholding among a large number of insiders again could potentially be an obstacle to efficient monitoring and could raise transaction costs. Opacity arising from fragmentation may be called Type II opacity. Finally (related to Type II opacity) is Type III opacity that could arise from the type of promoter shareholding, which can be classified into three distinct categories, namely individuals, listed companies, and unlisted companies and trusts. The more the weight of such shareholding is towards unlisted companies and trusts, the more it is unlikely for an outside minority shareholder, and even perhaps for outside members of the board of directors, to decipher chains of control as well as any related-party transactions. The ownership network becomes all the more complex if one considers additional cross-holdings by these private companies in group affiliates as is the case in many business groups.

Examining the different types of opacity for Indian listed companies, subsequent to the changed regulations since April 2006 which requires the identity of all constituents of promoters and promoter group along with their respective shareholdings to be disclosed under Clause 35, Type I opacity has almost been eliminated among listed firms. Prior to this period, the presence of such opacity had been documented by Sarkar and Sarkar (2008). However one finds considerable fragmentation of promoter holdings (Type II opacity) among listed companies—estimates across 3596 listed companies for March 2008 reveal that on an average a company has around twelve promoters, with the maximum across companies being as high as 46. Further, the mean (median) promoter shareholding within a company (a proxy for the extent of fragmentation) is only around 8 (5)%. Thus, while one finds significant concentrated ownership when all promoters are considered as a block, each promoter on an average has less than 10% shareholding. Given the data limitations, it is difficult to compute Type 3 opacity for all listed companies. Table 4 presents a detailed picture of Type 3 opacity along with the other manifestations of opacity for the flagship companies of the top four Indian business groups—Reliance Industries Limited of the Reliance Group, Reliance

Communications Limited of the Anil Dhirubhai Ambani Group (ADA Group), Tata Steel of the Tata Group, and Hindalco Industries of the Aditya Birla Group.

Table 4: Promoter ownership characteristics in selected companies (March 2008)

	Reliance Industries	Reliance Communications	Tata Steel	Hindalco Industries
A. Number of promoters by type				
All	48	11	16	19
Individuals	5	4	0	5
Listed Companies	0	1	5	7
Unlisted Companies & Trusts	43	6	11	7
B. % of holdings by promoter type				
All	50.95	66.13	33.94	31.43
Individuals	0.49	0.25	0	0.12
Listed Companies	0	0.89	5.23	8.05
Unlisted Companies and Trusts	50.46	64.99	28.71	23.26
C. Average promoter holdings by promoter type (B/A)				
All	1.06	6.01	2.12	1.65
Individuals	0.1	0.06	-	0.02
Listed Companies	-	0.89	1.05	1.15
Unlisted Companies and Trusts	1.17	10.83	2.61	3.32

Notes: 'A' lists the number of promoters constituting Promoters and Promoter Group as well as the number of each type of promoter (individuals, listed companies and unlisted companies and trusts). 'B' lists the total percentage of shareholding by promoter type, i.e., the percentage equity holding by promoters who are individuals, etc. 'C' is the average holding by type of promoter.

Source: Author's computations based on promoter shareholding disclosed under Clause 35 and reported in Electronic Data Information Filing and Retrieval System (EDIFAR) of Securities Exchange Board of India (SEBI).

As can be clearly seen from Table 4, the different manifestations of opacity (Type II and Type III) are in-built in the ownership structure of these companies, but to varied extents. Considering Type II opacity related

to fragmentation, Reliance Industries has as much as 48 promoters, with an equity share of 50.95%, which comes to be an average share of only 1.06% per promoter. The corresponding estimates for Hindalco Industries, Tata Steel, Reliance Communications are around 1.6%, 2%, and 6% respectively, all three lower than the average of 8% obtained for the total sample. Further, what is of interest is that more than 50% of the promoters belonged to unlisted companies and trusts of different types including investment trusts, the highest being for Reliance Industries, at nearly 90%. Among the other types of promoters, individuals are a distant second, and listed companies are nearly absent. With regard to the percentage of equity holdings by the three types of promoters, unlisted companies and trusts overwhelmingly account (80–90%) for promoter equity in the case of all four companies (as shown in Panel B).

5. Role of large blockholders in the governance of Indian corporates

The analysis of ownership structure in the previous section reveals the prevalence of concentrated promoter ownership and control in Indian corporates. This section discusses the impact of different blockholders (both insiders and outsiders) on firm performance in light of several large sample-based empirical studies and anecdotal accounts related to large shareholder activism in India.

Blockholdings in Indian corporates

The ownership estimates presented in Table 1 were arrived at by clubbing the individual shareholdings listed under each *type* of shareholder, without applying any cut-offs for individual blockholdings. In defining blockholdings, one of the most common cut-off points that is used in the literature is the legal definition of blockholders under Rule 13d-1(a) of the Securities Exchange Act of 1934 in the US, which sets the threshold for blockholding at 5% or more. In the case of India, additionally, the disclosure of equity holdings of 1% or more can be exploited to analyse the incidence of each *type* of inside and outside blockholdings in greater detail.

Table 5 presents the estimates of blockholdings in Indian corporates (as of March 2006) for blockholdings defined over different thresholds starting from at least 5% equity ownership to more than 75% equity ownership, all of which have strong institutional bases derived from existing corporate law and securities regulations, specifically the Companies Act (1956) and the Substantial Acquisitions of Shares and Takeovers (SAST) Act (1997). Table 5 also highlights the distribution of companies by the type of the largest shareholder following the major ownership classifications in Clause 35.[17] The 5% threshold in the Indian case also represents the minimum level of shareholding under the SAST (1997), when an acquirer has to disclose his/her shareholding to the target company and to the stock exchanges where the shares of the target company are listed. As Selarka (2005) points out, the 5% level captures the potential threat tof a takeover in the sense that the incumbent management is aware of the existence of a potential threat of a takeover. A minimum of 10% holding entitles a shareholder to sue the incumbent management with charges of oppression or mismanagement.[18] Also, shareholders with a minimum of 10% of paid up voting capital can call an extraordinary general meeting. Under the SAST Act (1997), an acquisition of 15% or more shareholding by a potential acquirer of a company requires a mandatory public offer by the acquirer of another 20% of the target company's share. A cut-off of 20% is typically the minimum level of equity ownership that is necessary to control a corporation (La Porta et al., 1999). Under the Companies Act (1956), a stake of 26% or more entitles a shareholder to block special resolutions and to have a say in the management of a company. A 51% gives majority stake and allows wide control over management of the firm but is subject to blocking minority; a stake of more than 75% is not subject to a blocking minority. Also, under the Indian Companies Act (1956), important corporate decisions such as proposed mergers, the buyback of shares, altering the memorandum and articles of association require 75% in favour. The highlights of the analysis of blockholders for different thresholds for a sample of 1965 listed firms for which disaggregated data was available in 2006, is presented in Table 5 and Box 2.

Table 5: Percentage of companies with different levels of blockholdings and type of largest individual blockholder (2006)

Type of Owners	Percentage of companies with equity ownership						
	>=5	>=10	>=15	>=20	> 25	>50	>75
Companies with a blockholder, the largest blockholder being	92.87	76.69	56.39	42.8	30.74 [85.4] {13.0}	5.65 [57.3] {6.0}	0.51 [22.2]
Indian Promoters	73.75	75.18	76.44	76.46	76.82	79.28	70
Foreign Promoters	6.08	6.9	8.93	10.58	11.92	16.21	30
PACs	7.62	7.23	6.32	5.83	4.8	1.8	0
Foreign Institutional Investors	1.09	0.73	0.36	0.36	0.5	0	0
Mutual Funds	0.22	0.13	0.09	0	0	0	0
Banks and Financial Institutions	2.36	2.26	2.17	1.78	1.49	0	0
Private Corporate Bodies	4.05	3.18	1.98	1.78	1.49	0.9	0
NRI/OCB	0.99	0.99	0.72	0.59	0.33	0	0
Indian Public	0.99	0.53	0.27	0.36	0.16	0	0
Any other	2.85	2.85	2.7	2.26	2.48	1.8	0

Notes: Estimates are based on 1965 listed companies. Estimates within square brackets are for Germany, and estimates within curly brackets are for the UK.

Source: Estimates for Germany and UK sourced from Kaserer and Moldenhauer (2005). Estimates for India are based on author's calculations of data from CMIE Prowess database.

To examine the extent to which outside blockholders (in particular institutional investors) can potentially act as a countervailing block vis-à-vis insiders, Table 6 presents the following three scenarios—(1) when all major types of institutional investors, i.e. FIIs, MFs and BFIs, act as distinct voting blocks with no coordination among them; (2) when domestic institutional investors (MFs and BFIs) coordinate their actions and monitor insiders as a single voting block, with FIIs acting separately;

and (3) when all institutional investors together act as a unified voting block. It is important to note that while the classification of outside blockholders has not undergone much change over the years, there has been considerable churning within each category of blockholder in terms of the functional and ownership status of its constituents since the nineties, so that it is a priori difficult to predict which of the alternate coalition possibilities would obtain.

Box 2: Characteristics of blockholdings in sample companies (2006)

- 93% of firms have at least one shareholder owning 5% or more equity.
- About 43% of companies have at least one shareholder with 20% control rights, which is the cut-off for effective control in many corporations.
- 30% of Indian firms have at least one shareholder who can act as a blocking minority, which lies in between the high 85.4% for 171 listed German corporations, and the relatively low 13% for the largest 173 listed UK corporations.
- Strong presence of promoters in Indian companies, irrespective of the level of blockholding; more than 70% of the companies have an Indian promoter as a dominant shareholder for any cut-off considered.
- On pooling both the direct and indirect holdings of all promoters, the percentage of companies with insiders as a dominant shareholding block increases further to at least 95% across all thresholds.
- The percentage of companies with foreign promoters increases as the threshold level of blockholding increases.
- Among dominant outside blockholders, the percentage of companies where a private corporate body is a dominant shareholder is the highest across all thresholds.
- The presence of institutional investors (particularly MFs and FIIs) as dominant shareholders is at most 1%, and almost absent at higher thresholds.

As is evident from the estimates of Table 6, the percentage of companies with outside blockholders under scenario 1 starts at around 46% for threshold levels of 5%, and systematically reduces by close to half for every consecutive change in the thresholds, to account for none for the thresholds crossing 75%. This is roughly the case for the other coalition combinations among institutional investors, although the corresponding percentages are noticeably higher with increasing thresholds when all

institutional investors are considered as a voting block. However, from the viewpoint of minority shareholders, even under this 'best case' scenario (i.e. under scenario 3), the presence of outside blockholders in the sample companies is barely 10% for thresholds of 20% or above, which simply means that only 10% of the sample companies have institutional investors as a potentially controlling block. Contrast this with the 86% of companies having insiders as a block holding at least 20% equity (as shown in Table 6). Also, increasing thresholds lead to a declining presence of each type of institutional investors, with domestic financial institutions not featuring as a blockholder in any company once the threshold blockholding touches 50%.

Table 6: Percentage of companies with insider and institutional blockholdings (2006)

Type of Owners	>=5	>=10	.>=15	>=20	> 25	>50	>75
A. Companies with inside blockholder	95.21	93.49	89.92	86.21	80.51	38.78	3.87
B. Companies with institutional investors as blockholders *with no coordination,* the largest institutional blockholder being –	46.00	23.91	11.14	6.36	3.61	0.20	0.00
(i) FIIs	8.96	5.70	3.21	1.83	0.71	0	0
(ii) Mutual Funds	3.71	1.27	0.51	0.20	0.10	0	0
(iii) Banks & BFIs	11.50	6.51	3.36	1.73	1.22	0.05	0
C. Companies with coordination *between domestic institutional investors only,* the largest institutional blockholder being -	46.67	25.34	12.42	6.92	3.91	0.25	0
(i) FIIs	8.45	5.34	3.15	1.83	0.71	0	0
(ii) Mutual Funds + Banks & BFIs	16.74	9.72	5.24	2.49	1.63	0.10	0
D. Companies with *coordination among all institutional investors with –*	47.33	28.40	15.27	9.87	5.75	0.25	0.05
companies having the institutional investors as the largest block among outside investors	26.56	18.47	11.40	7.33	4.17	0.10	0.05

Notes: Estimates based on 1965 listed Indian companies. FIIs = Foreign Institutional Investors; BFIs = Financial Institutions.

Source: Author's calculations based on data obtained from CMIE Prowess database.

Given the several estimates of the incidence of blockholdings in Indian corporates, the basic conclusion that can be reached is that promoters are in control in a large majority of listed companies, and the potential for institutional activism across Indian companies when measured by the extent to which institutional investors can act as a countervailing force against promoters through their blockholdings is at best weak. This picture somewhat improves when one considers the incidence and characteristics of multiple blockholdings in the top 500 companies, although the fundamental feature of disproportionate insider control still remains. Such control is further enhanced by management control by insiders as is evident from an examination of insider influence in the management of Indian companies. Estimates based on 307 of the top 500 companies in our sample for which both director-level data and ownership data were available show that about 67% of the companies in the sample have promoters either as a chairperson or as a managing director on company boards, with 69% of group affiliates and 63%of standalones having such directors on their boards. As can be expected, the promoters in these companies have controlling stakes which are on an average 50% (49% for group affiliates, and 51% for standalones).

A fall-out of the relatively low equity stakes of outside blockholders (particularly institutional investors), is that apart from curbing the incentives of these blockholders to monitor as hypothesised under the alignment hypothesis, it blunts the effectiveness of the 'exit' option that can be exercised by them as a governance mechanism. Instead, the exercise of the 'voice' option is typically exercised in India as in bank-based governance systems in Germany and Japan by virtue of holding significant equity positions and/or having substantial debt exposure. Almost all debt contracts with banks in India carry a covenant that it will be represented on the board of the debtor company via a nominee director (CII, 1998). This is often the case with institutional investors too (World Bank, 2005). The government-owned mutual fund, the Unit Trust of India, as well as government-owned insurance companies generally have nominees on company boards.

Blockholders and corporate performance in India

The overall picture that emerges from the preceding analysis of the incidence and trends in equity ownership of blockholders in Indian corporates is that of pervasive insider control which has persisted over the years despite some divestment taking place. Outsider blockholding levels which determine the potential for institutional activism in firms with insider control has not been substantial both in absolute and relative terms, when compared to the extent of insider control. In fact, insiders have monopoly control in a significant number of firms with institutional investors remaining a minority.

Several researchers have examined the relationship between large shareholders and corporate performance in the context of India, in the context of the conflicting theoretical hypotheses on the impact of insider and outsider blockholding on corporate governance. The challenge for existing empirical studies on the effect of large blockholders has been to capture the impact of blockholders on the governance of corporates in measurable units. Three strands can be broadly identified from the survey of the relevant literature, particularly with respect to the US, namely (1) studies that have examined whether the presence of blockholders, both insiders and outsiders, have influenced major corporate decisions such as executive compensation, leverage, and takeover activity (Holderness, 2003); (2) studies on outside blockholder activism that have estimated short-term stock market reactions to announcements of shareholder initiatives, and the voting outcomes on shareholder proposals (Gillan & Starks, 2007); and (3) analysing the "ultimate question" related to blockholders and corporate control, i.e. the relationship between block ownership (insider and outsider) and firm value including the effect of outside blockholder actions with respect to a targeted company on the long term performance of the company (Holderness, 2003; Gillan & Starks, 2007). In India, the focus has been on the ultimate question of the relationship between large blockholdings and corporate performance. The other two types of studies have not been much researched till date, mostly owing to data limitations.

Under the performance approach, the net effect of corporate governance is captured in terms of how particular governance mechanisms affect overall firm performance. This has been the predominant approach adopted in governance studies, particularly in the context of developing and emerging economies as well as other bank-based developed economies where discrete events are few and far in between. Both accounting and market measures are taken as measures of performance, with each of these measures having their own advantages and disadvantages. Accounting measures could have comparability problems if companies in a country do not follow uniform accounting standards, in which case market measures may be more appropriate. On the other hand, market measures may be less reliable compared to accounting measures in countries with inefficient stock markets. Various empirical studies take different calls on this issue choosing one over the other, whereas some studies use both measures to generate more robust conclusions.

The appropriate selection of a performance parameter is particularly challenging in the case of emerging economy studies with relatively underdeveloped stock markets, and less stringent and non-uniform accounting standards. With respect to market measures, most studies in countries with developed stock markets (like the US and the UK) use Tobin's Q and Market to Book Value Ratio (MBVR) as indicators of market measures of long term performance. MBVR is calculated as the ratio of the product of the number of equity shares and the closing price of the share on the last day of the financial year to the book value of equity and reserves. Tobin's Q is defined as the ratio of market value of equity and market value of debt to the replacement cost of assets. While no specific computational adjustments are needed to compute MBVR for emerging economies, the calculation of Tobin's Q becomes difficult primarily because a large proportion of the corporate debt is institutional debt that is not actively traded in the debt market. Also most companies report asset values to historical costs rather than at replacement costs. Thus the general practice in emerging economy governance studies that focus on market measures is to calculate a proxy for Tobin's Q by taking the book value of debt and the book value of assets in place of market values.

In general, market-based indicators are preferred to accounting indicators when analysing company value for at least three reasons. First, while accounting indicators incorporate only current information regarding the performance of the company, market-based indicators incorporate both current information as well as future prospects, and as such are likely to better reflect the overall financial health of the company. Accounting measures also have the potential problem of requiring a longer time to reflect the effects of governance. Third, market-based indicators reflect the valuation of the company by a large number of independent investors and are therefore likely to be more accurate than accounting indicators which may be subject to accounting practices specific to the company. Ideally, and under strict international accounting standards adopted by most developed countries, accounting indicators should be highly correlated with market-based indicators. However this is not necessarily the case in developing countries with reportedly low quality accounting standards (La Porta et al., 1998).

Box 3 presents a list of chronologically published empirical studies on the effect of large shareholders on firm performance in India. As can be seen from Box 3, the data-sets used in the studies have dated from the pre-reforms period (Chhibber & Majumdar, 1999), to several years into the implementation of governance reforms, i.e. 2004 (Pant & Pattanayak, 2007). Further the samples for all the studies except one have been drawn from the Prowess database, although differences exist among the samples in terms of their coverage. While some studies included only listed firms, others included unlisted firms as well; some included only manufacturing firms, others included both manufacturing and non-manufacturing firms. However, in terms of size, no sample is less than 1000 private sector firms, delineated by the different ownership groups. All the studies without exception have been conducted within a multivariate framework, examining the effect of different types of block ownership on firm performance after controlling for a host of other firm and market characteristics that are considered in the literature to influence firm performance. More recent studies (Kumar, 2008) have also taken into account the impact of possible endogeneity between ownership and firm performance.

Box 3: Summary of empirical research on large shareholders and performance in India (1999–2008)

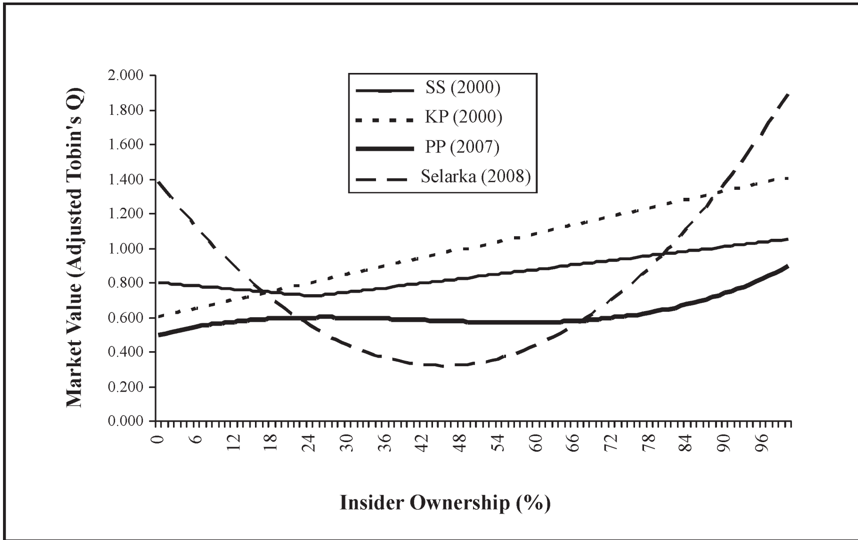
Paper	Sample	Firm Performance Measure	Variables of Interest	Findings
Chhibber and Majumdar (1999)	1001 private sector firms for pre-1991 and post-1991 period	Return on Assets and Return on Sales	Shareholdings by Foreigners	Foreign ownership has no effect on firm performance in the pre-1991 period. It positively affects firm performance in the post-1991 period but only after attaining majority shareholding of 51% or more.
Khanna and Palepu (2000)	Private sector listed firms for 1993	Market value of firm measured by Tobin's Q	Shareholdings by Insiders and Directors, Domestic Financial Institutions and Institutional Investors, Foreigners, and Top 50 owners	Foreign ownership has positive effect on firm performance. No effect of domestic financial institutions. Positive effect of insiders on firm value.
Sarkar and Sarkar (2000)	1567 private sector manufacturing firms for 1995–1996	Market value of firm measured by Market to Book Value Ratio (MBVR) and Tobin's Q	Shareholdings by Insiders and Directors, Corporate Bodies, Domestic Financial Institutions and Institutional Investors, and Foreigners	Foreign ownership has positive effect on performance. Insiders, corporate bodies and domestic financial institutions increase firm value beyond a threshold ownership of 25%. Domestic institutional investors have no effect on Tobin's Q, and negative effect on MBVR for ownership less than or equal to 25%.

Paper	Sample	Firm Performance Measure	Variables of Interest	Findings
Selarka (2005)	1397 listed manufacturing companies for 2001	Market value of firm measured by Market to Book Value Ratio (MBVR) and Tobin's Q	Shareholdings by Promoters (Insiders), and Outside Blockholders (Domestic financial institutions and institutional investors, foreign institutional investors and private corporate bodies	Insider ownership less than 46% has negative effect on MBVR, positive effect thereafter. Corporate bodies have negative effect at intermediate land high levels of ownership while blockholdings by banks and institutional investors have no effect.
Douma et al. (2006)	1005 private sector manufacturing firms for 1999–2000	Market value of firm measured by Tobin's Q and Return on Assets	Shareholdings by Insiders and Directors, Domestic Financial Institutions and Institutional Investors, Foreign corporations and Foreign Institutional Investors	Evidence of linear relationship between insider shareholding and firm performance.
Kumar (2008)	Unbalanced panel of 2478 listed manufacturing firms/5017 firm-year observations for the period 1994–2000	Return on Assets and Return on Equity	Shareholdings by Insiders and Directors, Corporate Bodies, Domestic Financial Institutions and Institutional Investors, and Foreigners	Foreign ownership has no effect. Domestic financial institutions and institutional investors with at least 15% stakes increase firm value. Positive effect on firm value for insider stakes of at least 24%.
Pant and Pattanayak (2007)	1,833 private sector listed firms/7330 firm year observations for the period 2001–2001 to 2003–2004	Market value of firm measured by Tobin's Q	Shareholdings by Promoters (Insiders)	Insider ownership less than or equal to 20% has positive effect on firm value; stakes exceeding 20% but less than or equal to 49% have negative effect on value. Stakes beyond 49% have positive effect on firm value.

With respect to the effect of insider ownership, the focus of several studies in the Indian context has been to examine the relative strengths

of the alignment versus entrenchment effects on firm performance, the former effect predicting a positive relationship between ownership and performance, and the latter a negative relationship. With the exception of Khanna and Palepu (2000), all the other studies postulate a non-linear relationship between inside ownership and performance to account for the possibility that the incentives of insiders, and the associated costs and benefits of the alignment and entrenchment effects change with their shareholding levels. While the ownership disclosure framework prior to 2000 allowed an examination of the effect of insiders as subsumed under managerial holdings (similar to the US studies) as well as family holdings (Douma et al., 2006; Khanna & Palepu, 2000a; Kumar, 2008; Sarkar & Sarkar, 2000), the later set of studies (using the post-2000 classification) sought to capture the effect of controlling insiders on firm performance as is usually defined in studies in non-US settings (Pant & Pattanayak, 2007; Selarka, 2005). The dominant picture that emerges from the existing body of evidence is that insider ownership and performance are non-linearly related to the relative strength of the alignment effect vis-à-vis the entrenchment effect, changing with changes in ownership. The indicative relationships obtained in some of these studies are presented in Figure 3. While support for a piece-wise linear relationship is found in both Sarkar and Sarkar (2000), and Kumar (2008) indicating that the benefits of the alignment or convergence of interests between insiders and outside shareholders outweighs the negative entrenchment effects once the promoter ownership crosses a threshold of around 25%, both Selarka (2005), and Pant and Pattanayak (2007) find a quadratic and cubic relationship respectively, which still supports the basic finding that the interests of controlling insiders and minority outsiders converge once insider control becomes sufficiently high.

Figure 3: Relationship between insider ownership and market value of Indian corporates—Results from select studies



Notes: To make a comparison of the qualitative relationship between insider ownership and firm value, the intercepts from the various studies have been normalised to the same value.

Source: SS (2000) = Sarkar and Sarkar (2000); KP (2000) = Khanna and Palepu (2000); PP(2007) = Pant and Pattanayak (2007).

With respect to outside blockholders, as is evident from Box 3 the empirical studies in the Indian context have exploited cross-section/time-series variation in outsider blockholdings in Indian companies (similar to the focus in other countries) to examine whether higher blockholdings by outsiders are associated with higher firm value (the efficient monitoring hypothesis), or are blockholders passive investors (the strategic alignment hypothesis), with no effect, or even worse, an adverse effect on performance. The latter possibility is suggested by much of the existing anecdotal evidence on shareholder activism in India.[20] Theoretically, shareholder 'activism' or the lack of it (shareholder passivism) is defined in the literature (see for instance, Black, 1990; Rho, 2007, among others) as the ability of outside shareholders to use the exit or/and the voice option to impact on the policies pursued by a company's management (Gillan &

Starks, 2007), and to broadly influence firm behaviour and governance rules (Black, 1998). Ideally, institutional shareholder activism should be captured in terms of the level of institutional activity with respect to interventions in board decision making and the like, and the resultant effect on corporate performance (as pointed out by Short & Keasey, 2005). However such data are in most cases not publicly available, and hence the level of institutional shareholding is taken as a reasonable proxy for the level of monitoring activity, the implicit assumption being that higher shareholding necessarily leads to higher monitoring, which translates into higher performance. Such issues should be kept in mind while interpreting the results of empirical estimation, and drawing conclusions from such research (Short & Keasey, 2005).

As is evident from Box 3, the evidence on the role of domestic institutional investors is mixed. Some studies which consider domestic financial institutions, insurance companies, and mutual funds as one block (Khanna & Palepu, 2000; Douma et al., 2006) find no evidence of the monitoring role of domestic financial institutions and institutional investors. The explanation of both Khanna and Palepu (2000) and Douma et al. (2006) is based on the fact that these investing institutions (during the period of their respective studies) were predominantly government-owned and hence did not possess either the incentives or the ability to monitor; the nominees of financial institutions may not have the experience or the incentive to be effective as their tenure and remuneration do not depend on the performance of their portfolio companies. Relaxing the assumption that all domestic financial institutions and institutional investors can be treated as a single block in view of the fact that the underlying motivation, and hence the monitoring incentives of these institutions are likely to be different (notwithstanding the government ownership of these institutions) Sarkar & Sarkar (2000) find that while institutional investors are passive monitors, for banking institutions, the firm value rises once these have substantial stakes (≥25 per cent) in companies. The mixed empirical findings on the governance role of financial institutions and institutional investors in India are not an exception when compared to the findings with respect to other countries (Black, 1998; Gillan & Starks, 2007).

With regard to the impact of foreign institutional investors on firm performance, the key result of the existing empirical studies on India is that foreign investors considered together have a positive effect on firm performance, although the debate is still on as to whether FIIs among them are active in governance. Anecdotal and survey-based evidence on FII activity in India in general suggest that FIIs are less passive than domestic institutional investors. As in the case of domestic investors, given the relatively small holdings of FIIs in a large number of companies, the potential for them to influence decision-making in companies through exercising the exit option is rather limited. FIIs in India are found to exercise the voice option relatively more than domestic institutional investors, through their attendance and voting at meetings, as well as through convening informal meetings with management. However like their domestic counterparts, FIIs are largely found to support incumbent management (World Bank, 2005).

The activism of FIIs in India came into sharp focus for the first time when, together with domestic institutional investors, they were successful in forcing Satyam Computer Services Limited to backtrack on the planned acquisition of two other group companies that had been approved a day before by its board (the plans were well within the law since it did not require a special resolution by shareholders). This was accomplished by offloading stocks over a window of just two days, during which the stock price of Satyam fell drastically, forcing the promoters of Satyam to call off the proposed acquisitions. Institutional activism mattered in the case of Satyam primarily due to institutional investors (particularly FIIs) having substantial equity in the company (around 48%) which together with the equity holdings of domestic institutional investors (around 13%) far outstripped the promoter holdings (around 9%).

While the Satyam case is considered as a watershed event in successful institutional activism in India and is consistent with the general finding of empirical studies that the effectiveness of monitoring by institutional investors increases with the increase in their holdings, ironically it is also an illustrative example of institutional passivism. When foreign institutional

investors as well as domestic financial institutions steadily increased their equity exposure in Satyam, the beginnings of the accounting fraud at Satyam took root. This could be interpreted as a sign of institutional passivism as one can argue that had the external blockholders (both domestic and foreign institutional investors) been engaged in continuous monitoring, the financial irregularities could not have built up over time. Although the investors were diligent enough to question the acquisition decision, what was also expected of them was their governing role in *ex-ante* prevention.

The conduct of institutional investors with respect to Satyam can be understood in light of the survey-based finding that institutional investors screen management of a firm *ex-ante* at the time of considering an equity investment in the firm, but once the investment is made, they support management decisions. It is only when they lose confidence in management due to 'discrete events' that they exercise the exit option (World Bank, 2005). The exit mechanism was effective in disciplining the Satyam management because of the large institutional equity position in the company and the coordinated action across the different types of investors.

6. Insider control and expropriation: Select evidence

While the complexity and opacity of ownership structures as seen in the Indian context can potentially result in Type II agency problems leading to expropriation of minority shareholders by controlling insiders, what does the evidence suggest?

As was discussed earlier, one of the key ways in which minority investor expropriation can be undertaken via the ownership structure of a firm is through tunnelling. Specifically, while the incentives for tunnelling in the Indian context lie in the pyramidal structures of business groups and the cross-holdings often amounting to circular chains of ownership, the ability to tunnel depends on a host of factors that include the opacity of ownership structures, the conduct of related-party transactions, the issue of debt, earnings manipulation, and internal capital markets for

intra-group borrowing/lending. Further, a crucial point is that while these characteristics create the incentives for tunnelling and hence the potential for minority shareholder expropriation, this does not necessarily imply the existence of minority shareholder expropriation. It is also important to note in this context that tunnelling by its very nature is clandestine, and hence cannot be easily deciphered and may not be conclusively proved (Bertrand et al., 2002. In fact, cases of tunnelling have usually come to light only after a corporate crisis—like with Parmalat in Italy, and Satyam in India. Whatever the scale of the failure and the diversion of funds through tunnelling for private benefits of control of insiders, minority shareholders suffer under all circumstances.

There have been essentially two sources of evidence across countries on minority shareholder expropriation—the first, an examination of individual cases following corporate collapses or due to allegations of complaints made and cases adjudicated, and the second, large sample empirical studies attempting to examine whether such expropriation exists via the various mechanisms of tunnelling. Both types of evidence exist with respect to Indian corporates. With regard to the first, specific cases of diversion of funds have been identified in recent years under the aegis of the Serious Fraud Investigation Office (SFIO) set up by the Government of India in 2003 to investigate financial frauds that involve public interest substantially either in terms of monetary misappropriation or in terms of persons affected (under the limits of the Companies Act, 1956). Between 2003 and March 2010, 767 cases of misappropriation and diversion were filed with the SFIO against 31 companies.[21] An examination of the nature of select cases under the SFIO based on information available in the public domain show that company promoters were in large part alleged to be instrumental in diverting funds and defrauding minority shareholders through various means. For instance the SFIO found that Daewoo India siphoned and diverted funds, manipulated accounts, and engaged in improper invoicing.[22] The Satyam fraud was the most serious of all the cases in India in recent times which involved the falsification of accounts (by the promoters) to the tune of around Rs. 7000 crore.[23] The Satyam

fraud also highlights how in concentrated ownership systems with insider control, the controlling shareholders have the power to indulge in self-dealing and to extract private benefits of control by manipulating financial transactions as well as financial statements, without the knowledge not only of the minority shareholders but also of the other members of the board of directors.

Apart from cases investigated by the SFIO, cases of shareholder oppression, mismanagement or apprehension of mismanagement of the company are adjudicated by the Company Law Board (CLB) in India under Sections 397/398 of the Companies Act, 1956. During the financial year 2008-09, a total of 931 cases under Sections 397/398 were placed before the CLB of which 186 were disposed off.[24]

With regard to the second source of evidence on the extraction of private benefits of control by controlling shareholders in India, there are only a few large sample studies which have empirically tested for minority shareholder expropriation especially in business groups. Based on an analysis of Indian business groups, Bertrand et al. (2002) find evidence of tunnelling—a transfer of resources from group firms in which promoters have low cash flow rights but high control rights at the bottom of the pyramid, to those where promoters have higher cash flow rights at the top of the pyramid. Based on a sample of 18,500 firm-year observations, the authors find that the profits of group firms exhibit lower sensitivity to industry shocks than standalone firms, and that this sensitivity is lower for firms where the directors' share (a proxy for shareholders' ownership) is low. The lower sensitivity of group affiliates suggests that the profit of a group firm low down in the pyramid and belonging to the particular industry responds less relative to a standalone (despite receiving a positive industry shock) possibly because the group firm transferred its unexpected increases in profits to its member firms. This conclusion is further strengthened by evidence that group firms' profits respond to shocks to other firms in the group belonging to unrelated industries, and within this set this sensitivity is higher in firms in which owners have higher ownership rights and accordingly higher benefits from tunnelling resources into these firms.

Among the other studies examining the phenomenon of minority shareholder expropriation are Saha (2010) which analyses the relationship between tunnelling and related party transactions (RPTs), and Sarkar and Sarkar (2008) which analyses the effect of ownership opacity on the incentives for minority shareholder expropriation through debt. The use of RPTs as a conduit for minority shareholder expropriation has increasingly been examined with respect to several emerging economies, including India. In India, the extensive data analysis of related-party transactions in Saha (2010) reveals that for a sample of 5394 Indian firms as of 2003–2004 and 2004–2005, group firms engage in such transactions with their holding companies to the tune of 25% of their assets as compared to only 2% for standalones, and with respect to parties in control to the extent of 30% of total assets as compared to 19% for standalones.[25] The differences in both the cases are statistically significant. Significant differences also exist with respect to the type of related-party transactions, particularly with respect to payables and receivables as well as the net credit lending (payables minus receivables), which are significantly higher for group affiliates relative to standalones. While RPTs in principle need not necessarily imply expropriation of minority investors and can instead be associated with enhancing efficiency in terms of lower monitoring costs vis-à-vis anonymous market transactions (Gordon & Palia, 2004), the evidence from select emerging economies as well as developed countries point to their use for the benefit of controlling shareholders. For instance, the collapse of the family-controlled Parmalat in Italy (a classic example of controlling shareholder expropriation to enrich family members) was perpetrated by family-controlled management and advisors through illicit RPTs with the company's offshore subsidiaries and special purpose entities (McCahery & Vermeulen, 2005).[26] Evidence regarding firms that belong to Chinese corporate groups also reveals that free cash flows have been diverted to controlling shareholders through RPTs (Jian & Wong, 2003). In India, the preliminary evidence on the relationship between RPTs and tunnelling does point to the association between tunnelling incentives and RPTs, and therefore the existence of minority shareholder expropriation (Saha, 2010).

With regard to the evidence of expropriation through debt in the Indian context, Sarkar and Sarkar (2008) highlight how the issuance of debt by controlling shareholders can facilitate expropriation of minority shareholders in their analysis of a sample of group-affiliated and standalone firms. As argued in the extant literature, with controlling insider stakes together with ownership complexity in terms of pyramiding and cross-holdings, debt can per se facilitate expropriation by enabling shareholders to increase their control over group affiliates. By increasing the proportion of debt relative to equity in the capital structure, insiders can have greater control over the resources of group affiliates without having to commit additional equity (Harris & Raviv, 1988; Stulz, 1990). This increase in control—transmitted through pyramids as well as cross-shareholdings—in turn can create more tunnelling opportunities for expropriating minority shareholders. Moreover, by issuing more debt in affiliates where they have low cash flow but high control rights, the controlling shareholders can potentially increase the resources that can be siphoned off from these affiliates through intra group loans, or transfer pricing to ones where their cash flow rights are higher (Faccio et al., 2001a; Ellul et al., 2006).[27] Large-sample evidence on expropriation through debt is found in Sarkar and Sarkar (2008) who (in their study of 1266 firms comprising group affiliates and standalones) test the hypothesis that higher levels of debt are associated with higher vulnerability of expropriation as measured by the different indicators of ownership opacity discussed above. The crux of their finding is that while opacity does not affect firm value for standalones, it is associated with a discount in value for group affiliates. Additionally, more opaque and group-affiliated firms with fragmented ownership structures are more leveraged.

7. Conclusion

The data analysis of the incidence of different types of blockholdings, and the detailed discussion of the empirical evidence on the impact of insider and outside blockholdings on firm performance since the mid-nineties lead to several important conclusions with policy implications.

The first is the pervasiveness of insider control in Indian corporates that has persisted over the years. While some firms have consolidated and some have divested their insider holdings, the overall picture has not changed much. Outside blockholders seldom have controlling stakes in corporates, or the ability act as a countervailing force against insiders, although the picture is somewhat better for larger firms.

With regard to the empirical evidence on the effect of inside blockholding, the common thread running through a majority of the studies is that the relationship between insider ownership and company performance is essentially non-linear, lending credence to both the alignment and the entrenchment hypotheses. While insider entrenchment and its adverse effects on company value are evident at low to intermediate levels of stockholdings, insider ownership has a positive effect on performance beyond a threshold. Outside blockholders can be a mitigating mechanism in the face of pervasive insider ownership and control, but the weight of the overall evidence with respect to governance by institutional investors is towards institutional passivity. The passivity of institutional investors at all levels of equity ownership strengthens the profile of institutional nominees drawn up in several accounts in the literature—nominees who seldom use the voice option as they have little expertise in the specifics of the company they monitor, and who have no risk of loss to bear if the value of an investment declines, and no reward to gain if the value increases.

In the face of institutional passivity in governance, and the potential for minority shareholder expropriation given the dominance of business groups with complex and opaque ownership structures (along with anecdotal and empirical evidence pointing towards such expropriation), governance reforms have been geared towards strengthening the voice mechanism of outside shareholders and facilitating low-cost exit. Reforms in the capital market for instance have involved institutional changes in both the primary and the secondary capital markets through the higher disclosures and reporting requirements in the listing agreement, the introduction of screen-based trading to ensure transparency in operations, the move towards nationwide integrated markets, the guaranteeing of all trades by a clearing house, and the dematerialisation of securities. Such

reforms have helped to increase market efficiency by helping investors to assess the true underlying performance of companies, and by reducing the costs of transactions, i.e. brokerage costs, market impact cost, paperwork, fraud and counterparty risk in the secondary capital market. In the context of the protection of minority investor rights, while provisions in the existing Companies Act (1956) have been considered to be at par with best-practice, the new Companies Bill (2009) has proposed the strengthening of existing laws even further through the provision of class action/derivative suits on behalf of depositors/shareholders that could force promoters and managers who are found guilty of misfeasance/fraud to pay the legal costs; it also highlights the need for proper and timely disclosures to safeguard the interests of the investors.

Given the pervasiveness and persistence of insider control, the moot point remains as to whether large shareholder oversight can in practice function as an effective governance mechanism in the Indian context (barring a few exceptional and isolated cases). The data analysis and empirical evidence in this paper reveals that given non-controlling shareholding, and little potential for increased consolidation in most cases, outside blockholders are likely to be ineffective on a continual basis through the exit and the voice mechanism. In such a scenario, the burden of governance—ensuring that controlling owners act in the best interest of all shareholders and do not engage in malfeasance—has to be borne disproportionately more by other internal and external governance mechanisms such as the board of directors, audit committees, and the market for corporate control.

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Notes

[1] The analysis in this paper omits from its purview the governance issues in state-owned enterprises in India. While several state-owned enterprises have gone for partial disinvestment and are listed companies, the control of these enterprises still lies with the government, and they are subject to the policy framework laid out by the government. The literature recognises fundamental differences and basic non-comparability in the governance problems of state-owned enterprises and private sector enterprises in terms of their maximisation objectives, their control structures, their employment and compensation policies, accountability, the extent of autonomy from government, and the like. Hence the governance guidelines for state-controlled enterprises are usually issued separately (see for example, GOI 2007; OECD, 2005).

[2] In firm D, the controlling shareholders are entitled to only 13% of the profits, while in firm A, the shareholders are entitled to 51% of the profits. Tunnelling allows the profits from firm D to be transferred to firm A (say through overcharging firm D on some goods or services) which while benefitting the controlling shareholders of firm A will adversely affect the minority shareholders in firm D.

[3] For instance, in the case of a poorly performing investment, the institution can dispose of its investment rather than try to pressurise the management to improve performance. While this would be an efficient monitoring mechanism in the presence of an active takeover market like tin the US and the UK, minority investment interests are likely to be adversely affected in countries without such a market.

[4] The listed firms belonging to the 'Z' category are excluded.

[5] PACs are identified based on specific definitions provided by SEBI (for example, in the case of an individual, PACs by definition include a promoter's spouse, parents,

brothers, sisters, or children, while in the case of a body corporate, PACs would include a subsidiary or holding company of that body corporate, or any company in which said body corporate holds 26% or more of the equity share capital. For further details, see http://www.sebi.gov.in/Index.jsp?contentDisp=Section&sec_id=1 (Accessed on 18 August, 2010).

[6] The term control was defined under regulation 2(1) (c) of the Act, and included the right to appoint a majority of the directors or to control the management or policy decisions "exercisable by a person or persons acting individually or in concert, directly or indirectly, including by virtue of their shareholding or management rights or shareholders agreements or voting agreements or in any other manner".

[7] This in turn is based on Explanations I, II, and III to sub-clause (m) of Clause 6.8.3.2 of the SEBI (Disclosure and Investor Protection) Guidelines, 2000.

[8] For further details, see http://www.sebi.gov.in/circulars/2006/dilcir132006.pdf (Accessed on 18 August, 2010).

[9] Prior to 2001, all foreign holdings (irrespective of whether these were promoter holdings or institutional investments) were clubbed under one category—"foreign owners."

[10] Individuals are further classified into those holding nominal share capital upto Rs. 1 lakh, and those holding nominal share capital exceeding Rs. 1 lakh.

[11] For instance, Claessens et al. (2000) recognise the problem of omission bias in the context of computing ownership data and tracing the ultimate owner in East Asian corporations. Of the 5284 corporations considered, the data for 1164 companies were missing or insufficient (covering less than one of the ownership rights). Lins (2003), analysing ownership structures in a cross-section of emerging economies, had to eliminate China and Poland from the sample on account of not being able to identify 90% of the blockholdings in half the sample firms.

[12] This is the standard cut-off applied in the literature to define widely-held firms (see Faccio & Lang, 2002; La Porta et al., 1998).

[13] Comparisons are based on the samples analysed in select European countries in Faccio & Lang (2002), in East Asian countries in Claessens et al. (2000), and in the US in La Porta et al. (1999).

[14] For a comparison of equity ownership of India with the other countries prior to 2001, see Sarkar and Sarkar (2000).

[15] A balanced panel of 2120 companies from the larger data set allows one to track ownership trends for any company for all six years.

[16] For instance, Goswami (2000) observes that in response to restrictions on private sector activities prior to the nineties, accounting and legal strategies were devised to ensure that business groups continued to control their companies while at the same time avoided high corporate and wealth taxes to the extent possible. This was achieved by owning companies, not through individual shareholding, but through ownership of trusts, small investment and finance companies, and through a complex web of indirect holdings.

[17] This exercise is fashioned along a similar exercise undertaken by Franks and Mayer (2001) to analyse ownership and control of German corporations.

[18] To reflect the interest of the minority shareholder, a 10% criterion is used for companies with share capital under Section 395 of the Indian Companies Act (1956).

[19] While there is a sizeable proportion of companies in which a corporate body represents the largest shareholder among blockholders (as shown in Table 6), the reason institutional investors are more potent as outside blockholders is that they often coordinate their actions and are more likely to act as a unified block than non-promoter corporate bodies, each of which is a distinct entity and may have different motives for holding relatively large equity positions in a particular company.

[20] See for example, World Bank (2005).

[21] For details, see http://www.sfio.nic.in/websitenew/in%20SFIO.pdf (Accessed on 18 August, 2010).

[22] For details, see http://www.financialexpress.com/news/serious-fraud-by-daewoo-37-m-sent-to-korea/120775/ (Accessed on 18 August, 2010).

[23] For details, see http://economictimes.indiatimes.com/infotech/software/Satyam-diverted-foreign-earnings-SFIO/articleshow/4422469.cms (Accessed on 18 August, 2010).

[24] Of the 931 cases, 355 fresh cases were received during 2008–2009. For details, see http://clb.nic.in/yrly2k8-2k9.htm (Accessed on 9 September, 2010).

[25] Saha (2010) notes that the total RPT as a percentage of total assets, aggregated across different categories constitutes about 74.67% in group-affiliates, and 34.53% in standalones.

[26] McCahery & Vermeulen (2005) add that the Parmalat case is not unique by itself, and several other companies with complex and opaque set-ups have emerged in continental Europe.

[27] Faccio et al. (2001a) argue that one of the reasons behind the high levels of debt precipitating the East Asian crisis was the “unmistakably” systematic expropriation by insiders via the use of debt, aided and camouflaged by ineffective capital market institutions, complex corporate pyramiding and extensive access to related-party loans.