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How do independent (Outside) directors' compensation structure, their frequency of meetings, and concentrated ownership effects shareholder's wealth? Evidence from Indian traded companies.

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Abstract

Purpose: This paper aims to confirm the effectiveness of Clause -49 (equivalent to Sarbanes –Oxley act of U.S.A.) of the stock exchange listing agreement to increase market stability and efficiency through new reforms in independent directors' compensation structure to help align directors' interests with corporate stockholders.

Design/Methodology/Approach: We used multivariate regression to examine the relationship between director compensation and firm performance. Data used are for two periods, 2005 and 2010, a sample of 260 firms from BSE-500 companies listed in India. This period includes two relevant times in the history of corporate governance regulation, representing an important event and crisis, making a nice variation to the analysis.

Findings: The findings provide some interesting insights into the relation between Independent director compensation and shareholders' wealth. First, an empirical study of Independent directors' remuneration from Indian firms adds significantly to the existing literature because most of the insights generated so far rely on U.S. data. Second, the research causes insights relevant to the regulation design of control structures that allow limiting the impact of sizeable inside ownership shareholder(promoter) on minority shareholder wealth. Third, the study refined the indicators to measure shareholder wealth. In other words, it throws light on who are the main enemies of shareholders' wealth?. It answers how one corporate governance variable, ownership structure, can influence the performance and efficiency of the shareholders' wealth.

Practical Implications/Limitations: The paper has high relevance for practitioner/regulator audiences.

Alternatively, what issue should regulators address to impact financial market activity more effectively through this ownership structure? It reflects how a decade-old corporate governance regulation can be detrimental to shareholders' wealth
The independent director's compensation fits well into current academic discussions that academics have shown less interest in understanding how non-executive board members get their compensation and how non-executive directors' remuneration affects firm performance?

Keywords: Executive Compensation , Corporate governance, Director, Independent, India, Outside, companies, Shareholders' value maximization

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1. Introduction: This study examines the effect of Independent (Outside) directors' compensation on firm performance (shareholders' wealth) in greater detail by identifying the form of director compensation (i.e., board sitting fees, commission, and salary) as well as the value of each type of compensation. Clause -49 of the Listing agreement at the Indian stock exchange defines an "Independent Director" as a non-executive Director of the company who:

a. apart from receiving the director's remuneration, does not have material pecuniary relationships or transactions with the company, its promoters, its Directors, its senior management, or its holding company, its subsidiaries, and associates, which may affect the independence of the director; b. is not related to promoters or persons occupying management positions at the board level or one level below the board; c. has not been an executive of the company in the immediately preceding three financial years; d. is not a partner or an executive or was not a partner or an executive during the preceding three years, of any of the following:

i. the statutory audit firm or the internal audit firm associated with the company, and ii. the legal firms and consulting firms that have a material association with the company; e. is not a material supplier, service provider or customer or a lessor or lessee of the company, which may affect the independence of the director; or f. he is not a substantial shareholder of the company, i.e., owning two percent (2%) or more of the block of voting shares; and g. he is not less than twenty-one years of age. Nominee directors appointed by an institution that has invested in or lent money to the company are also treated as independent Directors.

1.1Theoretical framework; According to agency theory, a potential problem exists when the ownership of a firm is separated from its management – as is typical of the modern corporation (Berle and Means, 1932; Jensen and Meckling, 1976). Because the owners (shareholders) are rarely involved in the day-to-day operations of a firm, it is difficult and costly for them to monitor a professional manager (agent) to ensure that the manager does not put his interests ahead of those of the firm's shareholders. Additionally, shareholders have little incentive to monitor because they would bear the entire cost and time, whereas all shareholders would accrue benefits (Porter, 1992). The regulatory pillars underlying executive compensation in India are clause 49 of the Listing agreement at Indian stock exchanges, which arguably sets the key normative parameters in this area. Black and Khanna (2007) noted that the announcement had far-reaching corporate governance reform in 1999; the introduction of clause 49 increased the stock price of large firms in India by around 4-5% over a three-day window of time. SEBI formalized the recommendations of the BIRLA committee in 2000 by including these as part of the Listing agreement's clause 49. Submission of the Murthy committee was later incorporated in 2006 into clause 49, ostensibly to apply lessons from the Enron scandal into the Indian Corporate Governance framework. Section IV (E) of clause 49 mandates that" all elements" of a director's compensation package be disclosed in the Annual report, including salary, bonus payments, stock option grants, pension contributions, as well as any other benefits (perquisites such as houses, cars, etc.). This disclosure requires to be accompanied by information regarding the fixed portion of the compensation package and details of performance-linked pay and performance criteria.

The scholars and practitioners recognized the separation of ownership and management and have stuck it through the years. In Volume III of *Capital* (1867), Karl Marx discussed the separation of ownership and control in a review of class structure, and Berle, Means published a three-book series on corporate governance in 1932 that coincided with the formation of the Securities and Exchange Commission in 1933. *The Modern Corporation and Private Property* (Berle & Means, 1932) documented the separation of ownership & control. Berle and Means, 1932, argued that the owner or shareholders of the firm exercised virtually no control over either day-to-day operation or long-term strategy and policy. Instead, control of the firm was given to professional managers who held very little ownership.
Jensen & Meckling (1976) defined the agency relationship as a contract in which one or more persons (principals) engaged another person (agent)to perform some services on their behalf, which involved delegating decision–making authority to the agent. The theory of the firm (Jensen & Meckling, 1976) suggested that it is necessary to encourage & protect specific investments, both tangible & intangible. The ability to protect these investments has been diminished by not having the motivation of management (the agent) and stimulation of owners (principals) in alignment.
Fama and Jensen (1983) thought that the problem was that managers and owners did not have an alignment of interest between the agent and the principal and that contracts were not written to the extent that can be enforced for transactions. The agency relationship can be reduced to agreements that provide safeguards for both parties to ensure that both sides fulfill their contractual responsibilities (Fame & Jensen, 1983). These contracts specify the rights of each agent in the organization.
Fame and Jensen (1993) suggested that contracts for corporate governance lacked enough substance to be enforceable. They thought that the process of contracting included a four-step decision process: (1) initiation of proposals for resource allocation, (2) choosing of initiatives to be implemented, (3) implementation of initiatives, and (4) Monitoring of agents' performance. Even though a contract may be written to outline the Usage of funds, contracts are generally flawed and incomplete and cannot cover the vast array of issues. Managers, therefore, end up with control rights or discretion over how an investor's funds. Professional managers are thought to have less incentive to maximize performance. As a result, workers' performance in the firm is more likely to decline than a presumed increase in performance in Owner-managed firms (Fama & Jensen, 1993).

2. Motivation of study: Research on corporate governance mechanisms dates way back to 1776, in the cornerstone writings of Adam Smith, in the "The Wealth of nation": "The directors of such companies (joint-stock companies), however, being the managers of other people's money than of their own, it cannot well be expected they should watch over it, with same anxious vigilance with which the partner in the private coparcenary, frequently watches over his own like the stewards of the rich man, they are apt to consider the attention to the small matters, as not for the masters honors, and very easily give themselves a dispensation from having it. Therefore, negligence and profusion must always prevail, more or less in the management of such affairs of such company". Adam smith's thinking predates numerous later scholars thinking on the incentives in the inter-personal and inter-organizational relations. Various groups, such as the National Association of Corporate Directors (NACD), have strongly promoted a diverse structure of director compensation. Still, the scarcity of research on director compensation suggests that further investigation is needed. Daily et al. (1999) point out.

There is virtually no evidence of a relationship between director compensation and a firm's performance. There is no consensus that we should even expect to see one. Ironically, while more significant stock ownership levels may cause directors' interests to align more closely with those of shareholders, significant ownership may also cause directors to lose some objectivity and independence. (p. 48).

Secondly, this study is relevant to the view

that academics have shown less interest in understanding how non-executive board members are compensated and what effect their compensation has on firm performance (Sarkar and Sarkar, 2012).

Hempel and Fay (1994) examine the relationship between board compensation and firm performance using the 1986 and 1990 proxy statements. They find little evidence of a relationship between director compensation and firm performance. However, most of the firms included in their sample compensated directors by paying them a cash retainer plus meeting fees. Additionally, due to data restrictions, the existence of a stock-based compensation plan was examined rather than the actual value of the stock plan.

In examining a sample of firms from 1992 through 1996, Bhagat et al. (1999) find no relationship between stock compensation and subsequent firm performance.

3. Model Specification: Accounting and stock market returns are widely reported measures of firm performance and have been frequently used in research [kren and Kerr, 1997]. This study employs a multivariate regression model to test the hypothesis regarding the effects of the composition of independent director compensation and concentrated ownership patterns on shareholders' wealth.

Hypothesis 1: There is a relationship between the structure of independent director compensation and shareholder wealth.

The accounting-based measure used for shareholder wealth in this study is – Earning per share (EPS) is defined as Profit After Tax divided by a Total number of equity shares issued for the years 2005 the year 2010, pooling data from the years 2005 and 2010 years of compensations are awarded.

Hypothesis 2: There is a relationship between corporate ownership structure and shareholders' wealth.

Accounting measures of shareholder wealth that are earning per share (EPS) were employed by Kesner [1987] and Kim et al. [1988] in their study because each measure has strengths and weaknesses in the evaluation as a performance measure for shareholders' wealth. The author assumes that market-based measures; it is possible that, even if director compensation can influence performance, there may be no correlation between pay and returns if the market fully impounds the director compensation information at the beginning of the period. Accounting–based measures offer a less noisy estimate of firm performance.

Hypothesis 3: There is a relationship between the frequency of independent directors' meetings and shareholders' wealth.

The specific regression takes the form:

Shareholders wealth= f (Structure of Director Compensation+ Control variable (Frequency of meeting, Industry, Promoters holding, institutional holding, Board size) +error

Where,
Shareholders' wealth= EPS= for the year 2005, the year 2010, and the panel of the year 2005 and 2010, the year in which the compensation is awarded, calculated as income before tax, extraordinary items, and discontinued operations divided by average total assets; Structure of Directors Compensation Includes= (Salary, Board Sitting fees, and commission)

4. Sample: The sample includes 520 observations-260 firms (see ANNEXURE-I) from the Bombay stock exchange-BSE-500 for 2005 and the *same* 260 firms for 2010. The firms were selected at random. If the firm had observations in both sample years and both samples–year observations met the data requirements, both years are included. The summary statistics of Independent director compensation observed by Sarkar and Sarkar(2012) for 2006, 2007, and 2008 were Rs. 2,72,000, Rs 3,26,000 and Rs. 3, 93,000 respectively. The compensation Variable matched with slight variation maybe since this data is of 260 companies for two periods for the year 2005 and 2010 from BSE-500 companies. From the top 500 companies, there is a period component to it.
As shown in Table 1, total independent director compensation averages Rs. 386 444(Median=Rs. 120000).In examining the sample by year (Table 2), it is apparent that Independent director Compensation policies have undergone major changes from the year 2005 to the year 2010.
Total Independent director compensation averaged Rs. 386 444 (Median=Rs 120000) in 2005, but increased to Rs. 5,46 ,973 (median= Rs. 200000) by 2010.

5. UNIVARIATE STATISTICS:

The sample consists of 520 firms' observations taken from BSE-500 firms. Two hundred sixty observations are from the year 2005and, the same 260 companies for the year 2010. Independent director compensation variables are for most Independent directors for the firm. Salary, Board sitting fees, and commission represent the value in Indian rupees. Total compensation is the sum of the board sitting fees, commission, and salary in rupees. The remaining variables are described below.

Table 1. Sample summary statistics

Variable	Mean	Median	Standard deviation
Compensation Variables			
Board sitting fees (Rs.)	97256	60000	114139
Commission (Rs.)	317318	0.000	804401
Salary (Rs.)	10340	0.000	220636.7
Total compensation(Rs.)	386444.3	120000	230560
Control Variables			
Net Sales.Rs.(In crores)	4781	1260	20649
Total Asset.Rs. (In crores)	11137	2056	38972
Corporate Governance Variable			
Board size	11.50	11	3.65
Institution Holding (%)	27.08	27.14	15.52
Promoters Holdings(%)	39.94	39.80	22.03
No. Of meetings attended	4.72	5.0	2.88

Data Source: Authors' compilation from the annual/balance sheet of 260 companies from BSE-500(see ANNEXURE-I).Note-1million=Indian Rs.10 lakhs; 1 US $=63 Indian rupees (Rs.) as on 12th December'2013: Indian Rs.10 Lakhs =Rs. 1million.:Indian Rs.1 crore=Rs.10 millions

Table 2. Sub Sample summary statistics and tests of difference of means

The last column provides the absolute value of the difference of means for the two sub-samples, 2005 vs. 2010, using the test of difference of mean, based on the Wilcoxon signed-rank test; for the definition of variables, refer to the above table 2 on summary statistics

		2005 Subsample			2010 Subsample		
Variable	Mean	Median	Standard deviation	Mean	Median	Standard Dev.	Diff. Mean
Compensation Variables							
Board sitting fees (Rs.)	87438	51000	108578.9	116535	84000	122098.7	16.87***
Commission (Rs.)	272436.9	0000	735978.2	405446	0000	918046.4	5.47***
Salary (Rs.)	10549.30	0000	220636.7	9931.324	000	248979	2.90***
Total compensation(Rs.)	386444.3	120000	840430.0	546973	200000	977836	17.91***
Control Variables							
Net Sales.Rs.(In crores)	4814.416	1201.865	21134.45	4716.599	1339.280	19670.26	10.31***
Total Asset.Rs. (In crores)	11381.95	2093.730	39769.28	10656.28	2018.076	37372.01	7.01***
Corporate Governance Variable							
Board size	11.49	11	3.669	11.51	11	3.621	2.95***
Institution Holding (%)	27.09	27.06	15.62	27.06	27.30	15.33	0.88
Promoters Holdings(%)	39.72	39.63	21.96	40.38	39.87	22.18	1.14
No. Of Meetings attended	4.69	4	2.91	4.775	5	2.84	8.87***

*** Indicates statistical significance at the .01 level, two-tailed **Indicates statistical significance at the .05 level, two-tailed * Indicates statistical significance at the .10 level, two-tailed

Data Source: Authors' compilation from the annual/balance sheet of 260 companies from BSE-500(see ANNEXURE-I).

Turning to the corporate governance variables, even though compensation has dramatically increased since 2005. While the board size remained the same, from 11.49 members in 2005 to 11.51 members in 2010, institutional holding remained the same from 27 percent to 27.06 percent by 2010.

In 2005, promoters holding made up 39.72%, while in 2010, it was 40.38%. By 2005, the no. of meetings attended by the Independent Director was 4.69, whereas, in 2010, it was 4.7. There were no other significant differences in the corporate governance variables in 2005 and 2010.

6. Empirical strategy/Analysis:

1) Relevance of the Year- Two factors have played a significant role in India; in the last ten years, corporate governance and the institution of independent directors have evolved. First, the introduction of Clause 49(considered equivalent to Sarbanes –Oxley act of U.S.A.) by the security exchange board of India (SEBI) in 2004 and the Satyam fraud in 2009 are considered necessary for improvements in corporate governance and the role of independent directors.

a) Justification for the Year 2005 data: Introduction of Clause 49 by the security exchange board of India (SEBI) in the year 2004 tempted the authors to go for the data of the year 2005 to see the impact of clause 49 (on Indian stock exchange listing agreement for Indian companies) on Independent director's compensations and shareholders wealth.
b) **Justification for the Year 2010 data:** The Satyam Company scam in 2009 had a significant impact. Dozens of independent directors resigned from several companies as responsibilities and risks of being a board member became clear. So, the author considered /assumed that in the year 2010, only those who were sure of their effectiveness continued as independent directors; another important thing that happened in the year 2010 was their compensation went up after this event.
So, in conclusion, after the Satyam scam of the year 2009, Clause 49 resulted in the induction of more independent directors and improvements in board processes. Boards meet more often as required by the regulations; it is assumed directors are speaking up in board meetings to ask substantive questions, voice concerns, and offer advice rather than just pop in cashew as in the past that is before the Satyam scam of 2009.

2) Regression Result:

A) Independent Director compensation:
Table 3 presents the regressions of Earning Per Share (EPS) for 2005,2010, and the total sample(the year 2005 + 2010) on Independent Director compensation. The models are not significant with $p < .01$. The adjusted R-squares are relatively low (Jensen and Murphy, 1990a, 1990b also report low R-squares), explaining slight variation in the EPS model. No independent director Compensation variables are significant in any of the EPS models.

B) Frequency of meeting:

Vafeas (1999b) finds that firms increasing meeting frequency experience improved performance. Specifically, he finds that boards meet more often following poor firm performance and that firm performance improves for these firms in the year after increasing the frequency of board meetings. This improvement in performance continues over the two and three years after the year of abnormal meeting frequency. However, Vafeas (1999b) examines firms that increase their board meeting frequency - presumably due to this poor performance. Alternatively, Hempel and Fay (1994) find no relation between the frequency of board meetings and firm performance.

Board meeting frequency was first defined as the log of the number of meetings (LMTG) and then as a dummy variable (DMTG) with the value of one for firms meeting seven or more times. In the EPS model, LMTG and DMTG are insignificant and negative.

Table-3, Contrary to Vafeas' (1999b) findings, firms with a high frequency of board meetings have lower performance following the observation year. Additionally, in the EPS model (Table -1), both LMTG and DMTG are insignificant.

Table-3 Compensation of Director, Frequency of meeting, and Corporate governance variables (EPS MODEL)

Regressions of Earning per share (EPS) on Independent Director Compensation, Industry control, t - statistics tests indicated in parentheses beneath the coefficients,

EPS for period

Independent Variable	YEAR 2005 EPS1	YEAR 2010 EPS 2	FULL SAMPLE EPS 3	FULL SAMPLE EPS 4
Regression	OLS	OLS	Fixed effect	Random effect
Intercept	11.2464*** (3.5815)	20.8954*** (4.1364)	13.286*** (5.07771)	13.1062*** (4.2733)
Compensation Variables				
Board sitting fees	-7.11E-07 (-0.1184)	-5.10E-06 (-0.5898)	-1.10E-06 (-0.2428)	-1.19E-06 (-0.2670)
Commission	8.28E-07 (1.3317)	4.09E-07 (0.4494)	7.37E-07 (1.4738)	7.19E-07 (1.4587)
Salary	1.76E-06 (0.7639)	8.83E-07 (0.2788)	1.59E-06 (0.9723)	1.55E-06 (0.9565)
Control Variables				
Net Sales	0.000123*** (4.4843)	0.000167*** (3.6188)	0.000178*** (8.4198)	0.000174*** (8.4033)
Total Asset	2.68E-05 (1.58188)	2.27E-05 (0.7900)	-3.21E-06 (-0.1869)	3.69E-07 (0.0218)
Corporate Governance Variable				
Board size	0.5123*** (3.0971)	0.2913 (1.0975)	0.5109*** (3.5069)	0.4779*** (3.2984

Institution Holding	0.04000 (0.9040)	-0.0370 (-0.5221)	0.0145 (0.3572)	0.00840 (0.2154)
Promoters Holdings (Founding and controlling /Dominant shareholders)	-0.0592* (-1.9201)	-0.11017** (-2.2424)	-0.0735*** (-2.7600)	-0.0780*** (-2.9850)
Log No. Of meeting attended##	0.1346 (0.049)	-3.2529 (-0.7237)	-1.5177 (-0.6947)	-1.4122 (-0.6474)
Dummy for more than six Meeting	-1.6103 (-0.8768)	0.2774 (0.0948)	1.3016 (0.9326)	0.9374 (0.6777)
AdjR^2	0.026	0.0177	0.1048	0.0279
F	6.6054***	2.866***	6.8998***	9.3815***
N(Companies)	260	260	520	520
No. Of Observation	1376	2860	4230	4230

*** Indicates statistical significance at the .01 level, two-tailed **Indicates statistical significance at the .05 level, two-tailed * Indicates statistical significance at the .10 level, two-tailed.

##The average firm in the sample met 4.06 times, and the median firm met four times.

Variable definitions:a)Net sales are the accounting figure from the company's profit and loss statement (in rupees) for the year compensation is awarded. b) Total asset is the accounting figure from the balance sheet (in rupees) of the particular company for the year compensation is awarded. c) Board size is the no. of the directors in the companies reported in the balance sheet of the particular companies for the year in which the compensation was awarded. d) Institution holding measured as a percentage of shares held by the institution as reported in the balance sheet for the year in which compensation was awarded. e)Promoters Holding measures the percentage of shares held by the promoters group as reported in the balance sheet for the year in which compensation was awarded .f)No. Of meetings measures the attendance of Independent directors as reported in the annual statement for the year in which compensation was awarded.

7. Discussion: Sarkar and Sarkar(2000) showed in the late 1990s, the average board size was smaller in India compared to the U.S., with 9.46 members on the Indian board compared to 11.45 members on the U.S. Board. While the percentage of inside directors was almost identical(25.38% compared to 26% in the U.S.), the Indian board had relatively fewer Independent directors (54%) compared to the U.S. (60%) and somewhat more affiliated outside directors(20% compared to 14% in the U.S.).Over 40% of Indian companies had a promoter on the board- and in over 30 % of the companies, the promoter served as chair. Sonja Fagernis (2007) reports that the average total compensation (salary plus commission of Indian C.E.O.s increased almost threefold between 1998 and 2004 from Rs. 21 lakhs(2.1 million) to Rs. Sixty-one lakhs(6.1 Million) in real terms. During this period, the proportion of profit-based commission to total pay also increased from 13.4% to 25.4%. The percentage of C.E.O.s as part of their compensation increased from 34% to 51%. Meanwhile, executives' compensation as a fraction of profit has increased from 0.55% to 1.06%. Ghosh. A(2006), in his studies during the period 1997-2002(a sample of 462 manufacturing companies), the average board compensation in India was around Rs.53 lakhs(5.3 million), with wide variation across the firm size.

The middle board compensation was Rs.76 lakhs(7.6 million) for large firms and Rs.25 lakhs(2.5 million) for small firms. Board compensation was also higher on an average of Rs.69 lakhs(6.9 million) when the C.E.O. was related to the founding family.

7.1 Reflection on the role of Independent (Outside) directors: On a personal note, the new Companies Act, passed by the government of India in the year 2013, has several additional provisions regarding independent directors, but the critical point is to reflect on whether the term "independent director" itself an oxymoron? How would the Independent directors justify their appointment to minority shareholders? What will be the qualifications criteria for independent directors to sit on the inboard of the companies? It will be interesting to see how this act passed in 2013 will also stand the test of time, how independent directors play their role as watchdogs on the promoters(Founding and controlling/dominant shareholders), and its top management protect minority shareholders' interests. The functions of these independent directors (as per clause-49, introduced by SEBI in the year 2004) are expected to perform to question various decisions made by the board, keeping in mind the interests of the society at large and also balancing it with the need for the company to survive and thrive. Primarily, they are expected to be unbiased, neutral, professional, honest, straightforward, and frank candidates and, most importantly, have a mind of their own. But, in a realistic world, it's a tall order.

7.2 How the independent (outside)directors are appointed: Given the fact that the promoters((Founding and controlling/dominant shareholders) of the company have the prerogative to appoint independent directors on the board of a company, the entire selection process reflects the purpose for which the appointment has been made: either it could only be made to fulfill the legal requirement, or it could be done to move towards ideals and give the power to independent directors to be the conscience keepers of the company so that the company gradually, but surely, moves towards higher business ethical values, legal compliance, and enhancement of social good. But that is what ought to be. In practice, unfortunately, the story is different. In the private sector companies, one has to be well known and trusted by the promoters to be invited to join the apex body of the company, that is, a board of directors as an independent director. In public sector companies, where the government is the promoter, these appointments are made not by the firm's chairman but by the minister in charge of the Public Sector Unit (P.S.U.). A lot of influence is required to become an independent director in a P.S.U.

7.3 Conflicting of interest, asymmetric information between Independent (outside) director and Promoter: Under this condition, how can an independent director be expected to be independent? Another point worth considering is that promoters and managements have far more information and knowledge regarding the affairs of a company/firm and have more resources than independent directors. The promoters and management also have more financial stake in decisions and, therefore, protect their interests vigorously. These make the job of an independent director very difficult, but not impossible. It will be interesting to see how independent directors execute their 'fiduciary' duty imposed under clause 49 towards minority shareholders! Under conflicting interests of promoters / top management on the one hand and independent directors, on the other hand, the role of independent directors in Indian companies will be variable of interest for years to come after 2013 not only to various stakeholders like shareholders, foreign investors, etc., as well to researcher's, practitioner's, regulator's, academician's more important to the lawmakers of India.

8. Conclusion: From the findings of this study, one can infer several things-with the introduction of Clause -49 in the year 2004 by SEBI, the capital market regulator in India; in theory, the role of independent directors was to bring objectivity to the board, protect the interests of minority shareholders, and improve risk management. So, the results (table-3) of this study suggest no relationship between the Independent director compensation structure and shareholders' wealth. First, *the compensation structure of the Independent director is not effective if seen from the stockholder's perspective, that is, the EPS Model mentioned in table -3.* Second, from the results (table-3), *there is no relation between the frequency of the Independent director's meetings and shareholders' wealth (EPS),* contradicting the finding of Vafeas (1999a:1999b). Which raises the question are independent directors speaking up in board meetings to ask substantive questions, voice concerns about minority shareholders, and offer advice, or do they pop in cashew provided by the firm in compensation? Thirdly, from table-2 and table -3, there is a *high agency cost in monitoring by independent directors in safeguarding minority shareholder rights.* Although, as can be seen from table-2, the total compensation of independent directors has increased to Rs.546000 (0.546 million) in the year 2010 from Rs.3,46,000(0.346 million) in the year 2005, which is about a 57% increase in total compensation from the year 2005, which has created no effect on the shareholders' wealth that is earning per share(EPS). Sarkar and Sarkar (2009) reveals in India marked level of concentration is in the hand of the "Promoters"(i.e., Founding and controlling/Dominant shareholders); they reported promoters own 50% of a sample of almost 2500 listed manufacturing companies. Sarkar and Sarkar(2000), as for the effect of concentrated shareholding on the company's performance, noted during 1995-96, holding above 25% by directors and their relatives was associated with the higher valuation of the companies.(while there was no clear effect below that threshold effect).Therefore, in such a high informatory asymmetry environment with greater ownership of promoters outside (independent) directors, monitoring and advisory roles are less efficacious (Duchin et al., 2010). The ownership concentration among a dominant shareholder (promoters-i.e., Founding and controlling shareholders) minimizes the risk of takeover. It, therefore, acts substitute mechanism for monitoring by independent directors (in the sample, see table-2, the promoters group/ Founding/dominant and controlling shareholders hold 40% of shareholding). A higher proportion of independent with high insider ownership further attenuates conflict of interest between them and the management/owner, hindering the decision-making process (Singh and Gaur, 2009). Another perspective for explanation is *ownership and control by promoters/ Founding /dominant and controlling shareholders*. The firm allows them to have their people on the board as an independent director. Sonja Fagernis (2007) also reports that C.E.O.s related to founding members or directors are paid more than other C.E.O.s. She also presents evidence that the presence of Directors from lending institutions lowers the pay. In contrast, more Independent directors on the board are associated with greater pay for performance to the insiders, which affects the other minority shareholders. In such cases, *the independent director role is more or less ceremonial and only for legal compliance requirement purposes*. This reflection is supported by the EPS model in table 3, where the compensation structure of the Independent director is not effective and promoters holding are negatively correlated with EPS and significant for all the four panels. Finally, from the economist's perspective, there is no linear pay-performance relationship, which prefers incentives throughout all performance levels and advocates fixed performance standards that discourage earning manipulations (Jensen and Murphy,2004). However, the absence of a linear pay-performance relationship between Independent director compensation and shareholders' wealth is to be seen with the high ownership of promoters. So it makes the role of independent directors uneffective when it comes to monitoring the promoter; as seen in table -3, the promoter's holding is negatively related to shareholders' wealth in all the models! *So, one can conclude that very high promoter's (Founding/dominant and controlling shareholder) holdings at the 40 % level negatively affect shareholders' wealth in all the models (table-3) of this study.* In the final analysis, what are visible the elements of corporate governance laid out in conventions, codes, and laws that have been strengthened over the years? As Adam Smith (1776) puts it that "the invisible hand" – guides the market, it is "the invisible spirit" that guides independent directors. So, let this invisible spirit guide the independent directors, who are "agents" - custodians of 'the promoter's and minority shareholder's money. Under the model corporation, law companies are artificial juristic and need natural persons to make decisions. Therefore, the conscience keepers of a company are the individuals managing the show. But it has not strengthened the spirit of corporate governance. The moral fabric of the company, as well as variation in shareholder wealth, are spun and woven by the major inside block holders(promoters). They are in control of the company's affairs. Unfortunately, statistics cannot measure and monitor this invisible spirit. The spirit lies in the hearts of the independent directors. It is rooted in the foundation of moral sentiments and values.

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"Science was first making a guess, then computing the consequences of that guess (building a model), and finally confirming or rejecting the guess with an experiment".

Richard Feynman, noble laureate physicist

ANNEXURE-I

Sample list of 260 companies selected from Bombay stock exchange (B.S.E.)-500 companies

3i Infotech	Blue Dart Exp.	Gateway Distr.	ING Vysya Bank	Maruti Suzuki	Shiv-Vani OilGas	Unichem Labs.
3M India	Blue Star	Geodesic	Ingersoll-Rand	Max India	Shoppers St.	Unitech
A B B	BOC India	Glaxosmit Pharma	Ipca Labs.	Mercator	Shree Cement	United Breweries
Aban Offshore	Bombay Dyeing	GlaxoSmith C H L	ITC	Monnet Ispat	Shri.City Union.	United Phosp.
Abbott India	Bosch	Glenmark Pharma.	IVRCL	Monsanto India	Shriram Trans.	United Spirits
ACC	Britannia Inds.	Godfrey Phillips	J & K Bank	MphasiS	Siemens	Usha Martin
Adani Enterp.	Cadila Health.	Godrej Consumer	J B Chem & Pharr	MRF	Simplex Infra	Uttam Galva
Agro Tech Foods.	Carborundum Uni.	Godrej Inds.	Jai Balaji Inds.	NCC	Sintex Inds.	UTV Software
Akzo Nobel	Century Textiles	Graphite India	Jai Corp	Nestle India	SKF India	V I P Inds.
Alfa Laval (I)	Cipla	Grasim Inds	Jain Irrigation	Neyveli Lignite	South Ind.Bank	Vakrangee Soft.
Alok Inds.	Clariant Chemica	Greaves Cotton	JBF Inds.	NIIT Tech.	SREI Infra. Fin.	Vardhman Textil
Alstom Projects	CMC	GTL	Jindal Poly Film	Noida Tollbridg.	SRF	Videocon Inds.
Ambuja Cem.	Coromandel Inter	Guj Gas Company	Jindal Saw	Novartis India	Sterlite Inds.	Voltas
Amtek Auto	CRISIL	Gulf Oil Corpn.	Jindal Stain.	Opto Circuits	Sterlite Tech.	VST Inds.
Amtek India	Crompton Greaves	H D F C	JM Financial	Oracle Fin.Serv.	Strides Arcolab	Whirlpool India
Ansal Properties	Cummins India	H F C L	JP Associates	Orchid Chemicals	Subex	Wipro
AP Paper	D C Holdings	Havells India	JP Power Ven.	Orient Paper	Sun Pharma.Inds.	Wockhardt
Apollo Hospitals	Dabur India	HCL Infosystems	JSW Holdings	Panacea Biotec	Sundram Fasten.	Zee Entertainme
Apollo Tyres	Deepak Fert.	HCL Technologies	JSW ISPAT	Pantaloon Retail	Supreme Inds.	Zuari Inds.
Aptech	Dewan Housing	HDFC Bank	JSW Steel	Patel Engg.	T N Newsprint	Zydus Wellness
Arvind Ltd	Divi's Lab.	HEG	Jubilant Life	Petronet LNG	Tata Chemicals	
Ashok Leyland	Eicher Motors	Hero Motocorp	Jyoti Structures	Pidilite Inds.	Tata Coffee	
Asian Paints	EID Parry	Hexaware Tech.	K S Oils	Polyplex Corpn	Tata Comm	
Aurobindo Pharma	EIH	Himadri Chemical	Kalpataru Power	Praj Inds.	Tata Elxsi	
Aventis Pharma	Elecon Engg.Co	Hind. Unilever	Kansai Nerolac	Radico Khaitan	Tata Global	
Bajaj Electrical	Electrost.Cast.	Hind.Construct.	Karnataka Bank	Rajesh Exports	Tata Inv.Corpn.	
Bajaj Fin.	Elgi Equipment	Hind.Oil Explor.	Kesoram Inds.	Rallis India	Tata Motors	
Bajaj Hindusthan	Emami	Honeywell Auto	Kirl. Brothers	Ranbaxy Labs.	Tata Power Co.	
Bajaj Holdings	Era Infra Engg.	Hotel Leela Ven.	Kotak Mah. Bank	Raymond	Tata Steel	
Balkrishna Inds	Escorts	I O C L	Kwality Dairy	REI Agro	Tata Tele. Mah.	
Ballarpur Inds.	Essar Oil	ICICI Bank	Lak. Mach. Works	Rel. Indl. Infra	TCS	
BASF India	Essar Ports	ICSA (India)	LIC Housing Fin.	Reliance Capital	Thomas Cook (I)	
Bayer Crop Sci.	Fag Bearings	IFCI	Lupin	Reliance Inds.	Timken India	
Berger Paints	FDC	India Cements	M & M	Reliance Media	Titan Inds.	
BF Utilities	Financial Tech.	India Securities	M R P L	Rolta India	Torrent Pharma.	
Bharat Electron	Finolex Inds.	Indiabulls Fin.	Magma Fincorp	Ruchi Soya Inds.	Trent	
Bharti Airtel	Fres.Kabi Onco.	Indian Hotels	Mah. Seamless	S C I	Triven.Engg.Ind.	
Bhushan Steel	G M D C	Indraprastha Gas	Mahindra Life.	S Kumars Nation	TTK Prestige	
Biocon	G N F C	IndusInd Bank	Manappuram Fin.	Sesa Goa	TVS Motor Co.	
Birla Corpn.	G S F C	Infotech Enterp.	Marico	Sh.Renuka Sugar	Uflex	

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