

# A Pre Companies Act and Post Companies Act comparison of Pharmaceutical Companies: A Corporate Governance perspective

Avtar Singh

Associate Professor and Head, Department of Commerce, G.T.B.National College, Dakha

---

## ARTICLE DETAILS

### Article History

Published Online: 20February 2019

### Keywords

Corporate Governance, Mandatory variables, Non Mandatory Variables, Voluntary variables, Industry specific variables.

---

## ABSTRACT

Over the last 30 years Corporate Governance has been a favourite subject of study among researchers. The researches are concentrated around five main themes, firm performance, corporate social responsibility, governance models, corporate disclosures and regulatory mechanism. Most of the studies are based in developing countries and are general in nature. Very few studies are related to a particular industry. The Companies Act 2013 could finally see the light of the day with its implementation. The focus of this Act was on Corporate Governance. Subsequently SEBI also brought about significant changes in its listing agreement in the form of SEBI (LODR). The present study is among the first, primarily on account of two reasons, one it makes a comparative analysis of the corporate governance levels prior to the Companies Act 2013 and after the implementation of the Act and two it is conducted on one single industry – the pharmaceutical industry.

---

## 1. Introduction

Corporate Governance, as a term gained currency during the last 30 years or so, but the word governance has been in circulation ever since the 15th century. Governance refers to the adoption of practices, procedures and rules to make decision making effective. The term is often used to refer to the quality of the functioning of an organization, be it governmental or non-governmental. The governance of companies is referred to as Corporate Governance.

Corporate Governance has witnessed a surge of developments in the last two decades, all over the world. India is no exception to this development. Various initiatives for the advancement of corporate governance in India have been made by the industry, Securities Exchange Board of India (SEBI), the Ministry of corporate affairs (MCA), and the professional bodies such as ICAI and ICSI since 1998. Superseding the archaic Companies Act of 1956 the Indian Government passed the Companies Act of 2013 which aims at enhancing Corporate Governance and Corporate Social Responsibility. Consequently, the SEBI also initiated various amendments to the listing agreement (clause 49) to make corporate governance more stringent.

## 2. Pharmaceutical Industry

The pharmaceutical industry in India has covered a long distance since 1970, when it was considered a small player in the Indian economy. Today this industry has given India place of eminence not only in the Indian economy but also in the world economy. This is evident from the events taking place during the times of Covid-19 and the development of a vaccine in India which is in high demand all over the world.

The value of the sector in India is estimated to be about \$4.5 billion and has a growth rate of 8% to 9% annually. There are 20,000 registered units out of which 250 large, 8000 small and 5 public sector enterprises. The government has permitted 100% foreign participation in the sector with permission to all inputs and products on a duty free basis.

## 3. Literature Review

The objective of review of literature is to cover most of the dimensions of corporate governance. It is intended to understand the various contours of empirical research and then to carry on the research in order to give a new direction to researchers, academicians, policy makers, investors and all other stakeholders.

**Abid. G, Khan. B, Rafiq.Z, and Ahmad. A, (2014)** have made a study to understand how various disciplines are influenced by corporate governance. They have studied and compared the various theories of corporate governance and hold the view that there a general theory of Corporate , should be developed which should be integrated with the legal system. **HeikoSpitzeck, (2009)** examined the relationship of corporate governance mechanism and the issue of corporate social responsibility taking a sample size of 51 organisations. The study found that organisations which have a corporate responsibility committee show better compliance of corporate responsibility. **Muneer Mohamed Saeed Al Mubarak, Allam Mohammed MousaHamdan (2016)**, evaluated how corporate governance and market capitalization are related on the basis of the Agency Theory. 36 firms listed on Bahrain Stock Exchange formed the sample. The time frame of the study was from 2009-13. The study has made use of econometric techniques to establish relationships between various dimensions of corporate governance and market valuation. **Marlene Davies Bernadette Schlitzer, (2008)**, studied whether 'one size fits all' approach can be applied to corporate governance. The paper concludes that such an approach cannot be considered the 'right approach from a global perspective'. **Mukhopadhyay, Mallik and Dhamodiwala (2012)**, constructed an index which consisted of four sets of variables – mandatory, non-mandatory, voluntary and beyond corporate governance containing 82 variables in all. The researchers used regression analysis. The study established that to improve financial performance of a company, it should improve levels of corporate governance. **Aggarwal, Reena,**

**Schloetzer, Jason D. and Williamson, Rohan (2015)**, studied the impact of revised corporate governance listing standards on firm value and corporate culture. It was revealed that the post mandate period was marked by a decrease in the value gap when compared with the earlier period. **Baysinger et al. (1991)** in their study examined the influence on R&D spending by factors such as percentage of outside directors on a company's board, equity ownership and the part played by institutional shareholders. The study found established that the quantum of R&D spending depended on two factors the role of institutional investors and the representation of insider on the Board. **Casper and Matraves (1997)**, studied the adaptability to change experienced by German and UK pharmaceutical firms. The authors opine that R&D is a part of national culture. **Lacetra (2001)** has highlighted the increasing importance being placed in the pharmaceutical industry on biotechnology and life sciences which has led to emphasis being placed on innovative activity. The author suggests a role for organizational practices on Corporate Governance and called for integration of governance mechanisms with innovative activity. The paper proposes industry oriented variables for pharmaceuticals which would include internal structure as well as relations with external parties.

An analytical study of the literature reveals that the work on Corporate Governance has undergone both a quantitative and qualitative improvement over the last 30 years or so. Research has been undertaken on a number of variables such as the impact of market efficiency, insider information, environmental performance, risk disclosures, equity holding pattern, R&D spending, human resource practices, etc. on Corporate Governance levels of companies. Most of the research has been undertaken in US and UK, some of the research is of cross national nature, few researches have been conducted in Indian conditions covering Indian regulatory framework. Even few researches have been conducted in industry specific conditions. It is widely recognized that there is need for more empirical research taking into account the Indian context. This it is believed can explore the institutional contextual realities of India (Padmini Srinivasan 2011).

#### 4. Organisation of the paper

The paper has been divided into five portions. The first portion relates to introduction, the second to theoretical perspectives and past research, third relates to research methodology, the fourth portion deals with analysis discussion and findings and finally the last portion relates to conclusion and directions for future research.

#### 5. Objectives of the study

1. To compare improvement in the levels of various variables mandatory, non mandatory, voluntary and industry specific during the Pre and Post Companies Act 2013 phases.
2. To compare the improvement in the level of corporate governance during the Pre and Post Companies Act 2013 phase.

#### 6. Hypotheses

A comparison of Pre and Post phases of the entire sample of 92 pharmaceutical companies has been made in order to evaluate the entire sample.

- **H0<sub>1</sub>**: The means of mandatory variables of the sampled companies for the Pre and Post companies Act period are equal.
- **H0<sub>2</sub>**: The means of non-mandatory variables of the sampled companies for the Pre and Post companies Act period are equal.
- **H0<sub>3</sub>**: The means of voluntary variables of the sampled companies for the Pre and Post companies Act period are equal.
- **H0<sub>4</sub>**: The means of industry specific variables of the sampled companies for the Pre and Post companies Act period are equal.
- **H0<sub>5</sub>**: The means of CG Scores of the sampled companies for the Pre and Post companies Act period are equal.

#### 7. The universe of the study

The pharmaceutical sector list of Bombay Stock Exchange displayed a list of 166 companies on the active list on 18<sup>th</sup> February 2014. The website Report Junction ([www.reportjunction.com](http://www.reportjunction.com)) which is a repository of Annual Reports of companies was evaluated to search for the reports of all the pharmaceutical firms. Since the data was not available for all the companies only those companies were selected which had data for the entire period. The data finally consisted of 92 companies (736 observations). The study involves the comparison of two time periods, therefore the data was grouped into Pre Co. Act 2013 and Post Co. Act 2013.

#### 8. Index formation

Most of the previous studies have taken recourse to indexes based on various parameters to quantify the extent of corporate governance. Two indexes for the Pre Co. Act 2013 period and Post Co. Act 2013 period have been framed. The rationale is that the Companies Act 2013, contains several new provisions specifically aiming to improve the corporate governance mechanism in India, a single index would not be adequate to calculate the level of corporate governance: Each of the variables within the sets have been measured on a five-point scale.

Most of the previous studies have taken recourse to indexes based on various parameters to quantify extent of corporate governance. Two indexes for the Pre Co. Act 2013 period and Post Co. Act 2013 period have been framed. The rationale is that since the in the Corporate Governance mechanism, huge changes have taken place because of the promulgation of Companies Act 2013, a single index would not be adequate to calculate the level of corporate governance: Each of the variables within the sets have been measured on a five point scale.

#### 9. Four sets of variables have been grouped in sub parts in both these indexes

**Set 1. Mandatory variables.** Every listed company is required to abide by certain guidelines as specified by the listing requirements specified by SEBI which have been subject to amendments from time to time. SEBI has powers to de list companies which do not adhere to the corporate governance norms and also penalize them.

**Set 2. Non-mandatory variables.** The clause 49 has included discretionary guidelines which are not compulsory provisions but it is desirable on the part of the companies to comply with these norms. The companies are required to disclose whether they have adopted the provisions or not and the reasons thereof in the Annual Report. The companies, listed on stock exchanges are required to report the observance or non-observance of these variables in the corporate governance section of the annual report.

**Set 3. Voluntary variables.** These variables have been identified from the Voluntary Corporate governance guidelines framed by Ministry of corporate affairs in 2009. The objective of the guidelines is that companies should move to a regime of adoption of voluntary rather than mandatory governance. The companies are expected to disclose the adoption or non-adoption to their stakeholders. Voluntary variables have been included in the CG indexes so that the extent of observance of the corporate governance can be adequately captured.

**Set 4. Industry specific variables.** Pharmaceutical industry has matured in a short time. Indian pharmaceutical sector ranks high in world rankings. While conducting research on pharmaceutical industry it becomes necessary to go beyond regulations and identify industry specific corporate governance

variables. The Annual Reports of five leading pharmaceutical Companies, Sun Pharmaceutical Industries Limited, AurobindoPharma Limited, Lupin Limited, Cipla Limited, Dr. Reddy's Laboratories were scanned to identify variables which could represent the industry. This was further supported by existing literature (Hajiheydari, Dastgir and Sultani 2011). Finally three variables were identified-Proportion of net profits spent on R&D, Scientists on Board of Directors and Committee on Innovation/R&D.

**10. Statistical tools used**

Test of homogeneity (Levine's test for equality of variances) has been conducted along with Dependent sample (Paired) t-test has been conducted. Descriptive statistics such as mean and standard deviation have been computed, Dependent sample (Paired) correlations have been found out.

**11. Comparison of all sampled companies**

A comparison of Pre and Post phases of the entire sample of 92 pharmaceutical companies has been made in order to evaluate the entire sample.

**Table 1**  
**Dependent sample (Paired) Statistics: Pre (All) vs Post (All)**

Pair	Variables	M	N	Std.Dev.	S.Err.M
P 1	PRE MV AVE	.61	92	.072	.007
	POST MV AVERAGE	.64	92	.083	.009
P 2	PRE NMV AVE	.39	92	.078	.008
	POST NMV AVERAGE	.41	92	.102	.011
P 3	PRE VV AVE	.32	92	.049	.005
	POST VV AVERAGE	.49	92	.077	.008
P 4	PRE ISV AVE	.27	92	.100	.010
	POST ISV AVERAGE	.29	92	.177	.018
P 5	PRE CG SCORE AVE	.46	92	.059	.006
	POST CG SCORE AVERAGE	.56	92	.073	.008

The Paired statistics reveals that the mean values of all the sets of variables and CG Score have improved in the post phase as compared to the pre phase. The following is an attempt to validate the results.

**Table 2**  
**Dependent sample (Paired) Correlations: Pre (All) vs Post (All)**

Pair	Variables	N	Correlation	Sig.
P 1	PRE MV AVE & POST MV AVERAGE	92	.609	.000
P 2	PRE NMV AVE & POST NMV AVERAGE	92	.225	.031
P 3	PRE VV AVE & POST VV AVERAGE	92	.430	.000
P 4	PRE ISV AVE & POST ISV AVERAGE	92	.574	.000
P 5	PRE CG SCORE AVE & POST CG SCORE AVERAGE	92	.648	.000

The statistics for the Dependent sample (Paired) correlations shows that all pairs of variables and the pair of CG

Score are positively and significantly correlated. The results of dependent sample paired tests is revealed thus.

**Table 3**  
**Dependent sample (Paired) Test: Pre (All) vs Post (All)**

Pair	Variable	Dependent (Paired) Differences					T	df	Sig. (2-tailed)
		M	Std.Dev.	S.Err.M	95% C.I. of diff.				
					Lower	Upper			
P 1	PRE MV AVE - POST MV AVERAGE	-.022	.069	.007	-.037	-.008	-3.084	91	.003
P 2	PRE NMV AVE - POST NMV AVERAGE	-.014	.114	.012	-.038	.010	-1.175	91	.243
P 3	PRE VV AVE - POST VV AVERAGE	-.170	.072	.007	-.185	-.156	-22.859	91	.000
P 4	PRE ISV AVE - POST ISV AVERAGE	-.018	.145	.015	-.047	.012	-1.163	91	.248
P 5	PRE CG SCORE AVE - POST CG SCORE AVERAGE	-.098	.057	.006	-.110	-.087	-16.585	91	.000

## 12. Analysis

### Pre MV vs Post MV

The means of mandatory variables are as follows: for Pre-Companies Act 2013 period (M=.61, SD=.072) and mandatory variables of Post-Companies Act 2013 (M=.64, SD=.083) under the conditions;  $t(91)=-3.084$ ,  $p = 0.003$ . Thus  $H_{01}$  was rejected.

### Pre NMV vs Post NMV

The mean values of non-mandatory variables are follows: for Pre-Companies Act 2013 period (M=.39, SD=.078) and non-mandatory of Post-Companies Act 2013 period was observed (M=.41, SD=.102) conditions;  $t(91)=-1.175$ ,  $p = 0.243$ . Thus the hypothesis  $H_{02}$  was accepted.

### Pre VV vs Post VV

The voluntary variables of the Pre-Companies Act 2013 period mean values (M=.32, SD=.049) differed significantly with the voluntary variables of the Post-Companies Act 2013 period (M=.49, SD=.077), when  $t(91)=22.859$ ,  $p = 0.000$ .  $H_{03}$  was rejected.

### Pre ISV vs Post ISV

The scores for industry specific variables are as follows: Pre-Companies Act 2013 period industry specific variables (M=.27, SD=.100) and Post-Companies Act 2013 period industry specific variables (M=.29, SD=.177) conditions;  $t(91)=-1.163$ ,  $p = 0.248$ .  $H_{04}$  was accepted.

### Pre CG vs Post CG

The CG Scores are as follows: Pre-Companies Act 2013 period CG Score (M=.46, SD=.059) and Post-Companies Act 2013 period CG Score (M=.56, SD=.073) conditions;  $t(91)=16.585$ ,  $p = 0.000$ .  $H_{05}$  was rejected.

## 13. Results

The aim of the study was to take the entire sample of 92 companies and study the extent of observance of the various variables of corporate governance.

The above statistical Analysis suggests that significant improvement can be observed during the post company act phase in terms of mandatory and voluntary variables and overall CG Score whereas no significant difference was noticed w.r.t. non mandatory and industry specific variables, although improvement has been observed.

## 14. Highlights of the study

When the entire sample of pharmaceutical companies is taken it is observed that by and large the companies have shown improvement in CG scores.

- The mandatory and voluntary variables have contributed to this improvement significantly.
- The improvement in non-mandatory and industry specific variables is not significant.
- The improvement recorded in the disclosure of mandatory variables is satisfactory.
- The improvement in voluntary variables is highly commendable.
- The overall CG score also shows a significant improvement.

## 15. Managerial Implications

The study of importance to the policy makers, investors, government and other stakeholders as it makes a comparison between the pre and post phases of the Companies Act 2013. The study reveals that the companies tend to pay more attention in demonstrating the mandatory variables as compared to other variables primarily on account of the increased penalties. The improvement in voluntary variables is significant and encouraging since the disclosures on this account is purely voluntary. The government should think of rewarding companies which show improved performance on this score. The improvement in the overall CG score shows that the change brought about the Companies Act has been well received by the corporate world. The low improvement of non mandatory and industry specific variables are a cause of worry. The government should encourage companies to disclose non mandatory variables. The low score on account of industry specific variables signifies that the pharmaceutical industry is paying less attention to R&D, appointment of scientists and formation of innovation committees.

## 16. Conclusion

Corporate Governance has come to occupy a place of significance in the corporate world. It is being increasingly realized that a lot of emphasis needs to be placed by companies on improving their levels of corporate governance to occupy a place of eminence in the corporate world. Realising the significance of Corporate Governance the

government of India implemented the new Companies Act 2013 from April 2014. The focus of the Companies Act is on enhancing the levels of corporate governance. Consequently the stock exchange regulator SEBI also brought about vast

changes in its listing agreement. The study was made to study the extent of change in the levels of corporate governance that may have come about because of these changes in the legislation and regulation.

## References

1. Aguilera, R. V., & Desender, K. A. (2012). "Challenges in the Measuring of Comparative Corporate Governance: A Review of th Main Indices", *Research Methodology in Strategy and Management*. Retrieved from <http://ssrn.com/abstract=1995616>
2. Anand, A. I. (2004). *An analysis of enabling vs. mandatory corporate governance: Structures Post-Sarbans-Oxley*, *Delawrare journal of corporate law*.
3. Anand, A. I. (2005). *Voluntary vs. Mandatory Corporate Governance: Towards an Optimal Regulatory Framework*. Retrieved from <http://law.bepress.com/espresso/eps/566>
4. Arya, P. P., Tandon, B. B., & Vashisht, A. K. (2003). "Corporate Governance", *Deep & Deep Publications Pvt Ltd, New Delhi*.
5. Baghdadi-Sabeti, G., & Serhan, F. (2010). "WHO Good Governance for Medicines programme: an innovative approach to prevent corruption in the Pharmaceuticak sector: compilation of country case studies and best practices", *World Health Report*. Retrieved from <http://www.who.int/healthsystems/topics/financings/healthreport/25GGM.pdf>
6. Baysinger, B., Kosnik, R. D., & Turk, T. A. (1991). "Effects of Board and ownership structure on Corporate R&D Strategy", *Academy of Management Journal*, 34(1).
7. Bebchuk, L. A., & Weisbach, M. S. (2006). "The State of Corporate Governance Research", *NBER working paper no. 15537*. Retrieved from [http://www.nber.org/papers/w15537.pdf?new\\_window=1](http://www.nber.org/papers/w15537.pdf?new_window=1)
8. Bhasin, M., & Shaikh, J. (2013). *Voluntary corporate governance disclosures in the annual reports: an empirical study*. *International Journal of Managerial and Financial Accounting*.
9. Cadbury, A. (1991). "The Financial Aspects of Corporate Governance", *Committee appointed by Financial Reporting Council, The London Stock Exchange*.
10. Fidler, A., & Msisha, W. (2008). *Governance in Pharmaceutical Sector*, *Eurohealth*, 14(1). Retrieved from [www.euro.who.int](http://www.euro.who.int)
11. Gopalsamy, N. (1998). "Corporate Governance - The New Paradigm", *Wheeler Publishing Co Ltd, New Delhi*.
12. Gray, S. J., & Skogsvik, K. (2004). "Voluntary Disclosures of Quoted Pharmaceuticals in Sweden and UK: The development over the period 1984-98", *European Accounting Review*, 13(4).
13. Gupta, A. (2015). *Compliance with Non Mandatory (Voluntary) Norms of Corporate Governance: Evidence from India*, *Indian Journal of Finance*.
14. Hajiheydari, A., Dastgir, M., & Sultani, A. (2011). *The effects of R&D costs on the profitability of Pharmaceutical companies*, *Interdisciplinary Journal of Contemporary Research in Business*, 3(8) (914-918 ed.).
15. Haldar, A., & Rao, S. (2013). *Corporate Governance Index for Listed Indian Companies*.
16. Khanna, U., & Madan, P. (2011). *Do Corporate governance practices differ across different market capitalisation of the firms: Some empirical findings from India?*
17. Lactera, N. (2001). "Corporate Governance and the governance of Innovation: The case of Pharmaceutical Industry", *Journal of managemnet and Governance*,
18. Mukhopadhyay, J. K., Malik, D., & Dhamodiwala, D. (2012). *Corporate Governance Practices and Financial Managed Medium sized listed companies in India*, *S.P. Jain Institute of Management and Research, Mumbai*. Retrieved from [www.nfcgindia.org/pdf/showcasing\\_corporate.pdf](http://www.nfcgindia.org/pdf/showcasing_corporate.pdf)
19. Murthy, N. N. (2003). "Report of the SEBI Committee on Corporate Governance". Retrieved from [www.sebi.gov.in/commreport/corpov.pdf](http://www.sebi.gov.in/commreport/corpov.pdf)
20. Post, J. E. (2009). "Never Waste a crisis": *Corporate Governance Reforms after Satyam Vikalpa*, 34(1).