Executive Compensation in Promoter Managed Firms in India

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This dissertation is dedicated to my wife, my best friend, my greatest supporter and a constant source of joy, Gayathri Susarla, who had enough strength to pull me up every single time I was about to give up, while fighting some of the life's toughest battles herself.

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Abstract

During the last decade, several Indian listed companies have faced significant backlash over excessive compensation awarded to their promoter executives, often seen as misaligned with the company's financial performance. In 2018 for instance, Apollo Tyres was severely criticized from the business media, proxy advisory firms and shareholders over high compensation of the promoters Onkar Singh Kanwar and his son Neeraj Kanwar despite the firm's operational challenges and market volatility. Similarly, in 2021, Eicher Motors experienced shareholder discontent when Managing Director Siddhartha Lal's salary was proposed to be raised to ₹21.13 crore. In 2019, Balaji Telefilms faced criticism for high pay packages awarded to the Managing Directors Shobha Kapoor and Ekta Kapoor. Critics were unhappy about the disproportionately high pay packages, given the company's volatile financial performance and rising costs. Sun TV Network's Kalanithi Maran also sparked controversy for earning ₹77.92 crore in the fiscal year 2016-2017, with his wife Kavery Kalanithi drawing a comparable amount, leading to intense debates on executive compensation in promoter-led firms. Broadly, these stories underscore the ongoing concerns about excessive promoter compensation and the critical need for aligning promoter executive pay with the financial health and performance of the company, ensuring that the minority shareholder interests are safeguarded.

However, promoter led firms in Corporate India are not without some shining examples of promoter executives taking a conservative and balanced approach to compensation. For example: the Chairman and Managing Director of Reliance Industries, Mukesh Ambani's decision to cap his annual salary at ₹15 crore since 2008 stands out as a model of restraint and governance. It's the same case with Anand Mahindra, the Chairman of Mahindra & Mahindra, Harsh Mariwala of Marico, Kiran Mazumdar-Shaw of Biocon, and Narayana Murthy of Infosys. These executives stand out as beacons of 'promoter accountability', and demonstration of responsibility towards minority shareholders' interests.

Public discourse in the business media widely highlighted that promoter CEOs are taking disproportionately higher pay packages compared to their professional counterparts and that it was an indication of excessive managerial power exerted by promoter CEOs on the boards. Several business articles raised the curiosity in me to investigate the facts and trends behind the topic of

promoter CEO pay through research, and specifically investigate the linkage of pay to firm performance. In this endeavor, I also noted that there is a lot of academic research published on this topic that effectively supports the managerial power theory, nepotism in family run businesses, and gross asymmetry in the pay vs. performance relationship, specifically during the high performing and low performing years for the promoter CEOs. Largely, these studies argued about promoter CEO's compensation as a mechanism for some controlling families to tunnel corporate resources.

I was intrigued by these narratives, and wondered 'how much is too much', especially when it comes to the compensation of promoter executives? These companies being public listed companies, it is essential for minority shareholders from the retail and institutional segments to gain a data-based view to the compensation decisions to cast their votes as part of the Annual General Meetings (AGMs) every year. Therefore, I chose to explore and investigate the pay vs. performance linkage of promoter CEOs, using compensation data of S&P 500 companies from 2013-2021. Specifically, I investigated the 'linkage of promoter executives relative to their professional counterparts. Interestingly, contrary to my initial conjectures, my findings do not seem consistent with the observations made by the business media and academia (referenced above). Broadly, what I found is that the pay levels of promoter CEOs are indeed higher than professional CEOs; but this 'pay' demonstrated higher sensitivity to the performance delivered by them vis a vis their professional firm counterpart. Under the 'total salary terms', promoter CEOs are paid 30% higher than professional CEOs. The fixed component is comparable between the two, but the commission component is significantly higher for promoters directly contributing to the higher total compensation. This indicates that the boards/NRCs link a significant portion of the promoter CEO compensation to the 'commission' component of the pay. I show through this study that the commission component of promoter CEOs has stronger linkage to firm performance when evaluated against a stringent industry peer group adjusted 'return on assets' as the performance measure, which is a widely accepted performance metric as used in multiple academic research works. Additionally, I also found that promoters are effectively penalized on their commission component when the performance results are lower, thereby reinforcing the linkage between pay and performance. This finding directly contradicts the

widely held narrative on this topic and surfaces a new finding, which could be a matter of interest for industry practitioners, academia and the boards.

In 2013, the Indian government introduced major revisions in the Companies Act; it was a watershed moment in the Indian corporate governance landscape. Through this study, I show a secular change in executive compensation trends, influenced by proactive policies in the Companies Act 2013, and subsequent expert committee recommendations on board composition and disclosure standards. Finally, I recommend several policy changes to pay disclosure standards, aimed at democratizing investing to empower minority shareholders by providing easy access to quality information, enabling them to make informed decisions on compensation-related proxy proposals.

Practitioner/ Policymaker Implications: the findings from this research highlight the currently prevailing disclosure standards that are causing potentially incorrect narratives in the minds of minority shareholders on executive compensation, influenced by third parties and business media, who may not have the resources, skills and time to conduct a thorough data-based research. It is due to the inherent difficulty for retail shareholders to be able to consume the facts from the compensation disclosures made by the firm and its relation to firm performance. Policymakers need to intervene by formulating more definitive and stringent norms for firms to disclose executive compensation, specific performance measures used by the firm and showing the linkage between the compensation awarded to the specific performance goals achieved, in plain English for the benefit of the minority shareholders. The disclosures need to be in a form that is readily comprehensible to a retail shareholder unambiguously. Such policy interventions would help establish a disclosure environment that is conducive to good governance, and directly contribute to higher participation of retail shareholders in the decision-making process for corporate India.

Keywords: Executive compensation, Corporate Governance, Disclosure quality, promoter compensation, Pay vs performance

1. Introduction and Motivation

Executive compensation of corporate India has been a topic of interest and is increasingly becoming a key issue in the constantly evolving corporate governance landscape. Large Indian-listed businesses historically had concentrated promoter-family ownership. Most of these firms also have a family member as the CEO and/or as the chairperson of the Board. Moreover, it may be noted that a lot of research has gone into analyzing executive pay packages, albeit in the context of western markets; but there have comparatively been limited studies that have explored/analyzed compensations of Indian CEOs, with particular emphasis on promoter vs. professional CEOs. Most of such publications, including articles in business newspapers, highlighted that promoter CEOs of India are taking higher pay packages relative to their professional counterparts. Such works explained this phenomenon with the managerial power theory, demonstrated through nepotism, captured boards, disproportionate allocation of pay with performance.

My research on this topic may be attributed to this backdrop, and the widely held market / media view that promoter managers' pay is disproportionally higher. When I collected and analyzed the compensation data of top 500 listed companies by market capitalization from India's National Stock Exchange (NSE) covering the time period 2013-21, my findings at large, did not support the initial hypothesis that was based on the dominant view of the market. I found clear counter evidence to the above widely held narrative. In this dissertation, I present my research design, and investigate the construct of pay vs. performance.

In addition to the quantitative examination of the compensation components, and their relationship to firm performance factors, such as profit, sales, return on capital, return on equity etc., I incorporate the view of practicing professionals from the industry in the form of qualitative interviews with industry experts, board members, compensation consultants as well as proxy advisory firms. Practical insights from these industry professionals would help understand the board room dynamics, competition in the executive leadership talent pool, influence of various practical factors that might be playing an important influential role in the determination of executive compensation. Their insights and observations would be helpful for examining the issues from a 360-degree perspective, particularly for understanding the unique conditions when promoters or their family members also play the managerial role in firms.

The primary motivation for my research in this subject is driven by the question about the availability and transparency of key data points related to executive compensation to minority shareholders as part of the disclosures mandated by the Indian regulators. Executive compensation section in the annual reports of the listed firms provides details on the pay packages of executives, but it is grossly insufficient to be able to provide a clear information to the minority shareholders on the executive's pay packages and their relationship to the performance benchmarks / measures used for these awards. Minority shareholders, in the absence of time and resources available to them to conduct their own data analytics on the pay performance relationship, lean into the narratives provided in the journalistic media, and such articles provide a view, based on the level of analysis they could do with the data made available in the disclosures. When it comes to pay vs. performance analysis, the disclosed information and the data is highly inadequate to establish specific measures used by the company to refer to the concept of ‘performance’. I took up this research to examine data that is made available in the annual reports of listed companies on India’s National Stock Exchange (NSE). I collected a wide range of firm performance measures and indicators, evaluated the pay vs. performance relationship for both promoters and non-promoter CEOs to test the real relationship between them, and compare it with the widely held narratives in the press. Broadly, we note some of the important and urgent needs to bring in several reforms related to quality disclosures on the aspects of pay and performance, to a degree that it helps minority shareholders to consume this information without a need for advanced data and analytics skills or depend on the commentary provided by third party sources for an opinion. Notably, such quality disclosures with detailed data on the pay-performance relationship is pivotal to a truly democratic decision-making within the corporate governance process involving minority shareholders.

Based on the learnings from my research, exploring the gaps between perceptions and facts when it comes to evaluating the pay-performance relationship for promoter CEOs, I also make a series of recommendations for policymakers on improving the disclosure quality of compensation data and decisions, solely for the benefit of minority shareholders. Such quality disclosures by firms help in easier understanding and consumption of data by minority shareholders without a need for onerous analytical work and skills that may not be readily available to them. Notably, such easy-to-understand and high-quality disclosures are essential for inviting the participation of retail shareholders in the corporate governance process, and for upholding the true spirit of good governance.

2. Ownership Structure and Role of Promoters

An important and rather unique aspect of Indian corporate ownership in the documents of incorporation involves the term ‘promoter’. Later in this dissertation, under a separate section on corporate governance framework of India I provide a detailed definition of the term ‘promoter’ as defined by the Companies Act. Broadly, it refers to an individual or a group, who are the (co)founders of a firm, and bring significant capital; hence, become the controlling shareholders. More than half of the listed companies in India are promoter-owned, and the companies in which, promoters hold more than 50% of stake in ownership has increased from 56% in 2001 to 66% in 2018. Promoters continue to wield a significant control over their firms’ day-to-day working as well as the strategy. This has a direct impact on other stakeholders including institutional, retail, and other minority shareholders.

Dominant ownership by promoters brings a combination of pros and cons, both to the corporation and the economy at large. Promoters, as the original ‘owners’ of the firm bring the required capital, managerial oversight and other resources to the firm creating the much-required stability and long-term sustainability. In the Indian context, many promoter-driven firms are named on their family names, which creates a strong family identity and psychological bonding for the well-being of the corporation, resulting in long-term sustenance of the brand and the firm, generating value for all stakeholders.

On the contrary, if the dominant promoter ownership is not governed well, it has proven, in some cases, to be detrimental to the minority shareholder interests. This is when the promoters place their self-interests and gains at the expense of the corporation and other stakeholders. Market regulator SEBI and the Ministry of corporate affairs introduced rules to ensure adequate governance and oversight with relevant policies around board composition, restricting related party transactions, stringent disclosure requirements on securities pledging, and other key matters to protect the interests of minority shareholders. Disclosures related to the compensation and benefits offered to the executives and strengthening the composition of NRC with higher presence and participation of independent directors is a step in that direction.

3. Literature Review

Executive compensation is a topic that is extensively researched over many decades from multiple viewpoints. An extraordinarily rich literature base is already available; most of which, focus on studying executive compensation from the Anglo-American corporate governance viewpoint. Limited studies focus on this topic from the point of view of emerging economies like India. The following section reviews some of the major theories that shaped the regulations around executive pay so far.

3.1 Optimal Contracting Theory

Executive compensation has been analyzed using the classical Agency theory with the objective of reducing costs associated with the misalignment of interests of the principals (shareholders) and the agents(managers) appointed by them to run the operations of a firm (Jensen and Meckling, 1976, Eisenhardt, 1989). The Agency theory was proposed under the fundamental assumption that agents are risk-averse, opportunistic, and self-centered; their interests may not be aligned with those of the principals. Hence, the model inherently consisted of the 'Moral Hazard' problems, when the agents could take excessive risk on the firm with the objective of higher personal gains, while the principals bear all the costs of such risks. Similarly, the problem of 'adverse selection' refers to the agent being better informed of their abilities than the principal at the contracting time. Several mechanisms have been implemented; for instance, pay alignment of agents with the gains of the principals to address the moral hazard and adverse selection problems. The body of knowledge encompassing these ideas is the 'Optimal Contracting theory', which attempts to strike an appropriate balance between the agent's and principal's interests, using the fundamental elements of 'base pay' and an 'incentive pay' (Jensen and Murphy, 1990). Several innovative mechanisms have been developed on these theoretical foundations to improve the alignment between agents and principals, such as stock-based compensation, stock options, multiple forms of long-term incentive plans, etc. This theory implies that compensation practices found in practice tend to benefit the minority shareholders through the alignment of managers' incentives with theirs.

3.2 Managerial Power Theory

The Managerial power theory challenges the optimal contracting view by raising its shortcomings with questionable independence of the boards, and the executives' influence over the appointment of directors, and the benefits resulting in captured boards. This theory primarily focuses on the view of managers gaining excessive control to the extent of working against the interests of the principals. Rent extraction, short-term performance focus over long-term wealth is typically evidenced in such scenarios (Bebchuk, Fried 2004). From the executive pay perspective, Bebchuk and Fried (2004) provide an elaborate study and findings of the observable patterns of the managerial power in their work 'Pay without Performance' such as camouflage of rents, usage of compensation consultants to justify higher pay than to optimize it. Frydman and Jenter (2010) noted that the managerial remuneration saw a steady rise from the 1970s to 2000s much more than the rank-and-file employees and explained the pattern with increased managerial power as a significant determinant of the of executive pay. Bebchuk and Grinstein (2005) provided detailed empirical evidence of the disproportionate increase of the pay relative to firm performance between 1993 to 2003, and the role played by the equity-based compensation plans in causing this negative effect. Kevin Murphy (2012) presented the negative role played by disclosure regulations, tax policies, and accounting rules related to stock options, and how managerial power presented itself in worsening the pay-performance linkage. PM Guest (2010) in his study of board structure and executive pay, established the relationship between the proportion of independent directors in the boards of UK firms. The author identified that higher percentage of independent directors have a negative relationship with the executives' pay rise. Practices such as 'peer group benchmarking' employed by the compensation consultants contributed to less efficient pay packages by opportunistically selecting the peer groups (Bizjak, Lemmon, et al, 2008). From the Indian context, Chakrabarti, Subramanian et al., (2011) identified a positive relation between executive remuneration and the size of the firm measured by a composite factor of market capitalization/assets/sales. They also reported a positive relation between the CEO's pay and the proportion of promoter's holdings. Chen et al., (2021) reported that the promoter managers pay was asymmetrically linked to the high performing vs. low performing firms. They found that the promoter managers are paid higher compensation during the years when the performance of the firm is higher; and in contrary, they are not paid lower during the low performing years. Study of the data from a sample of 277 publicly listed Indian family firms during 2004–2013 reveal nuanced heterogeneity of nepotism in emerging economy family firms. The study argues that CEO compensation is a mechanism for some controlling families to tunnel corporate resources. This body of work also supports the view that the governance mechanisms fail to prevent dominant managers from awarding themselves excessive compensation.

3.3 Focus of my work and the gaps from prior Research

The Indian corporate environment has a unique ownership pattern, where a significant portion of the public listed firms' ownership and control lies in the hands of the promoters. This presents a unique dynamic, which cannot be explained solely by the optimal contracting or managerial power theories as explained in the previous two sections. Furthermore, as outlined under the literature review section, there are numerous papers written from the western context of executive compensation, highlighting multiple patterns, while demonstrating the managerial power in action. Although there are limited number of works in the Indian context, many of the Indian papers have shown that promoter CEOs demonstrated their power in drawing higher pay packages due to their control and power on the firm and boards, exerted through their ownership. This has been related to the managerial power theory and nepotism, due to the induction of multiple family members on the boards and as executives. However, there is a limited body of work that focuses specifically on the trends of the Indian executive's compensation, and thereby evaluate the impact of the improved disclosure and regulations on the pay patterns especially in the recent past (i.e. after the launch of major revision of the companies Act in 2013). My approach is focused on evaluating the pay levels with a specific emphasis on its sensitivity to the performance delivered by the promoter and professional managers. Also, much of the quantitative research on the promoter vs. professional CEO compensation has been done using compensation data from years prior to 2013 (Chen, Chittoor, & Vissa, 2018). I wanted to take an objective approach to evaluate a relationship between the executive's pay and a wide range of performance measures to question if there was evidence for disproportionate allocation of pay packages for promoter CEOs relative to professionals. In my research, I followed a similar approach adopted by Chen, Chittoor, & Vissa, (2018), using industry level median adjusted excess return which is considered as a widely accepted pay-performance linkage assessment mechanism. However, as part of my research, I validated the arguments, using compensation data from 2014 to 2020, during which, there have been significant regulatory reforms on board compensation, compensation structures, and the increased governance controls placed by the boards for public companies. There is also a marked increase in the quality of data disclosure of compensation as part of the annual reports, post 2013 reforms of the companies act. My analysis of the pay performance linkage significantly deviates from the trends noticed from the data patterns prior to 2013. Boards have demonstrated a shift towards linking a significant portion of promoter executive compensation to the commission component, which in turn, is driven by the performance delivered by the firm. However, the results also surfaced gaps in the disclosure quality of annual reports, which is not helping a retail shareholder understand the data and facts behind the pay performance linkage without engaging in complex analytics. Such a low-quality disclosure environment is not conducive to inviting higher retail shareholder participation in matters of corporate governance. This paper highlights the gaps in the difficulty of interpreting and assessing the pay performance linkage for minority shareholders from the annual disclosures made as per the prevailing regulations and makes recommendations to improve the quality of these disclosures for better transparency and comprehensibility.

4. Corporate Governance Framework in India

This section summarizes India's corporate governance framework, along with the major revisions applied to it post 2013. This is relevant in the context of my work, whereby I examine the same, and look to make inferences of the changes in composition, and the pay patterns of promoter managers following the introduction of these regulatory interventions. Notably, much of extant research in the Indian context presented a case of managerial power in action by the promoter CEOs. My research is going to evaluate these arguments by examining the pay-performance relationship of promoter and professional managers from S&P 500 listed companies from 2013-14 to 2019. The following section provides the context of the key regulatory interventions that shaped the evolution of governance reforms between 2013-2019.

The core entities responsible for defining the organizational framework for corporate governance in India are the Ministry of Corporate Affairs (MCA) and Securities and Exchange Board of India (SEBI). With the recommendation of the Bhabha committee, the companies Act 1956 was introduced. Several amendments to the Act were made in 2002 with the constitution of National Company Law Tribunal replacing the Company Law Board. Another major change was shifting from democratic voting rights to the Plutocratic voting rights for shareholders, which brought about a change of one vote to one share as opposed to one vote to one member. Year 2013 is described as a watershed moment for corporate governance reforms in India. In the year, the Indian government introduced the Companies Act 2013, replacing in the process, the old companies act 1956. The changes introduced in the Act 2013 have far-reaching implications to significantly change the manner in which, corporates operate in India. This section covers the highlights of the key reforms / changes introduced into the corporate governance landscape by several committees appointed by the Government of India and SEBI over the last two decades, particularly in the context of public listed companies.

4.1 Companies Act 2013

1. The term 'promoter' has been defined as
    a. a person who has been named as such in a prospectus or is identified by the company in the annual return referred to in Section 92 of 2013 Act that deals with annual return; or

b. who has control over the affairs of the company, directly or indirectly whether as a shareholder, director or otherwise; or

c. in accordance with whose advice, directions, or instructions the Board of Directors of the company is accustomed to act.

2. Section 149(1) introduced requirement of having at least of one-woman director on the Board.
3. Section 149(3) extended the limit of maximum number of directors to 15; however, it can be extended beyond by passing a special resolution. Minimum number of directors is 3.
4. Incorporation of the aspects from SEBI Clause 49 into the Act itself - every public- listed company to have at least one-third of the total number of directors as independent directors. SEBI requires that if the non-executive chairman is a promoter or related to promoter of the company, one half of the board needs to be consisting of independent directors.
5. Independent director is not eligible to get stock options, but may get payment of fees and profit linked commission subject to limits specified.
6. section 150 introduced the appointment process of independent directors by constituting a panel or a data bank to be maintained by MCA, out of which, companies may choose their independent directors.
7. Section 149(12) provided immunity from any civil or criminal action against the independent directors. The intention and effort to limit liability of independent directors is demonstrated with a note on their obligation - "only in respect of such acts of omission or commission by a company, which had occurred with his knowledge, attributable through board processes, with his consent or connivance or where he had not acted diligently."

8. Introduced the mandatory requirement of constituting the nomination and remuneration committee by every listed company.
9. Transactions entered into with related parties are included in the board's report along with justification for entering into such contracts and arrangements.
10. The re-appointment of a managerial person cannot be made earlier than one year before the expiry of the term instead of two years as per the 1956 Act.
11. Section 196 revised the eligibility criteria for the age limit for appointment of KMP to 21 years from 25. The upper limit of 70 years can be extended by passing a special resolution.
12. Listed companies are mandated to disclose in their board report, the ratio of remuneration of each director to median employee's remuneration.
13. The 2013 Act has liberalized the administrative procedures by relaxing the requirement of obtaining the central government's approval, provided the company complies with certain requirements, including seeking approval by way of special resolution for payment of managerial remuneration.
14. Section 198 outlined in detail about the allowances and deductions that a company should include while computing the profits for the purpose of determining the managerial remuneration.
15. Section 203 stated that an individual cannot be appointed or reappointed as the chairperson of the company, as well as the managing director or chief executive officer of the company at the same time, except where the articles of such a company provide otherwise.

16. The overall ceiling in respect of payment of managerial remuneration by a public company remains at 11% of the profit for the financial year, calculated in the manner laid out in section 198.
17. Remuneration payable to anyone managing director or whole-time director shall not exceed 5% of the net profits. Remuneration of all directors and managers taken together shall not exceed 10% of net profits. However, these limits can be extended by passing a special resolution.

4.2 The Kumara Mangalam Birla Committee 1999 (Clause 49)

1. Appointed by SEBI with an objective for the committee to suggest amendments to the listing agreements executed by the stock exchanges with the companies to improve corporate governance.
2. Independent director defined as a non-executive director (other than a nominee director), who has no pecuniary relationship with the company apart from the remuneration, no relationship to the company's promoters, directors, and management.
3. Number of independent directors should be one-third in case of a non-executive chairman on the board, and at least half in case of an executive chairman.
4. Audit committee to have at least 3 directors, all being non-executive with majority being independent.
5. Mandatory Remuneration committee on the board to be comprised of at least 3 non-executive directors with the chairman being an independent director.
6. Board meetings shall be held at least 4 times a year with a maximum gap of 4 months between two meetings.

7. Non mandatory: Chairman's role in principle be different from the CEO.
8. Introduction of postal ballot for increased shareholder participation in voting.
9. All pecuniary relation of non-executive directors to be disclosed in the annual report.
10. Detailed disclosure of director remuneration (all elements of compensation including salary, benefits, bonus, stock options, fixed and performance linked incentives along with performance criteria) in the corporate governance section of the annual report.

4.3 The Naresh Chandra Committee 2002

Consequent to the several corporate scandals in the USA followed by the stringent enactments of Sarbanes Oxley Act, the Government of India appointed the Naresh Chandra Committee in 2002 to examine and recommend amendments to laws pertaining to auditor-client relationships, and the role of independent directors. Key recommendations are as follows:

1. The minimum board size of all companies as well as unlisted public limited companies with paid-up share capital and free reserves of Rs. 100 million and above, or turnover of Rs. 500 million and above, should be seven, of which at least four should be independent directors.
2. No less than 50% of the board of directors of any listed company as well as unlisted public limited companies with a paid-up share capital and free reserves of Rs. 100 million and above or turnover of Rs. 500 million and above, should consist of independent directors.

3. Certain services are prohibited to be provided by an audit firm that cause a conflict of interest with an audit client.

4.4 The N.R. Narayana Moorthy Committee 2003

SEBI constituted a committee under the chairmanship of N.R. Narayana Murthy, chairman and mentor of Infosys, with a mandate to review the performance of corporate governance in India and make appropriate recommendations.

1. All audit committee members shall be non-executive directors. They should be financially literate and at least one member should have accounting or related financial management expertise.
2. Audit committees to mandatorily review financial statements, and management discussions; they should analyze financial results, risk reports, related party transactions etc.
3. Exclusion of nominee director from the definition of independent director
4. Limits to be defined on the remuneration of non-executive directors including stock options, disclosure of level of stock holding by the non-executive directors annually and also prior to the appointment.
5. Companies need to affirm that they provide the personnel access to the audit committee of the company and 'whistle blower' protection policies are incorporated in the policies.

4.5 The Uday Kotak Committee 2017

The SEBI Committee under the Chairmanship of Mr. Uday Kotak along with different stakeholders from the Government, industry, stock exchanges, academicians, proxy advisors, professional bodies, lawyers etc., was formed in 2017 with the aim of improving standards of corporate governance of listed companies in India. Following are the key recommendations of the committee as approved by SEBI with certain modifications:

1. Minimum of 6 directors on the board, increased from the minimum of 3 from the companies act '13.
2. At least one women independent director on the board.
3. Role of chairman and MD cannot be played by the same person (SEBI extended to be in effect from April 1, 2022).
4. Directorship in listed companies limited to 7 per director, to avoid the busy director related concerns.
5. Minimum remuneration for independent directors as 5 lacs per annum and sitting fees of 20,000-50,000 for each board meeting.
6. Independent directors need to be free from Board interlocks.

5. Executive Compensation Related Regulations

Executive compensation has been a topic of wide debate in developed economies for several decades. In India, the executive compensation of public companies has been restricted by government regulations and limits, and hence did not reach to levels to draw attention of shareholders. Moreover, it may be noted that India's economic liberalization of 1994, essentially opened up its economy to the global marketplace; it enabled attracting, retaining, and compensating executives of Indian firms so that they could keep pace with the global competitiveness of Indian firms. It was also at this point that compensation levels of Indian executives witnessed a stupendous rise. A sample study of Kakani and Ray, (2002), exploring large Indian firms found that the growth in the Indian executive compensation was about four times that of the growth of the remuneration of rank-and-file employees. The authors rightly observed that the 2005-2006 period may be identified as a watershed moment for corporate governance reforms in India. The Securities and Exchange Board of India at this point, also introduced Clause-49, which provides detailed guidance on board composition, structure, and heightened disclosures both in case of executives as well as the board's compensation. Clause 49 also requires that public listed companies disclose the detailed compensation structures including key management persons' fixed pay, performance-linked variable pay, along with other benefits in their annual reports.

A major enhancement to corporate governance in India was introduced in the form of the Companies Act 2013, which mandated the creation of Nomination and Remuneration Committee (NRC) for every public listed company. It was also mandated to have at least one half of the NRC with Independent Directors, with the objective of having the board play an objective and impartial role in determining the compensation levels and the structure of the executives. Promoter CEOs and directors as interested parties are also prohibited to participate and vote in such decisions to influence the compensation levels and structures. If implemented in spirit, the proposed regulations should help implement compensation structures that bring about a closer alignment of executive interests with those of the shareholders.

5.1 India specific Agency Problems / Promoter Driven Firms

Majority of large Indian listed companies have been historically controlled by ‘promoters’ or business groups that enjoy considerably higher control rights and cash flow privileges than those of the other shareholders. This gives rise to a new type of agency conflict, which is different from the principal-agent conflicts. Conventional executive compensation theories have been based on resolving the principal-agent conflict by designing compensation schemes that aim to align the interests of agents to that of the principals. However, due to the nature of Indian companies’ ownership and control structures, a significant number of executives and board members come from the promoter’s families or from the business group that has higher control rights on the decisions of the firm. This situation gives rise to different agency conflicts that are termed as ‘horizontal agency costs’. Monitoring and controlling these horizontal costs are way more expensive compared to the vertical agency costs; Fagernas(2006), Jaiswall and Firth(2007). Moreover, given the closer alignment of owner-managers with that of other shareholders, it is intuitive to expect that the compensation packages of promoter executives to be lower than that of the professional executives.

6. Research Questions

When I started developing a working hypothesis for my research, I was heavily influenced by many publications, including articles in business newspapers, which highlighted that Indian promoter CEOs are taking away higher pay packages relative to their professional counterparts, and that it was excessive. Several of these newspapers and articles argued that promoter CEOs may be taking an undue advantage of their power to take higher pay packages. In fact, many of these articles explained this phenomenon with the Managerial power theory, demonstrated through nepotism, captured boards, disproportionate allocation of pay with performance.

My research on this topic started with this context as the backdrop, and the widely held market / media view that promoter managers pay is disproportionally higher. However, what I found was that there was limited Indian literature available, linking executives' compensation to performance, especially within the ambits of promoter vs. professional CEOs. In fact, even in these works, the data available was very limited, possibly because most of those studies were done prior to the revised compensation disclosure rules from SEBI (i.e. prior to 2013). Moreover, the data quality did not provide a clear classification of performance linked pay components. Besides, the results of many of those studies with limited available data were no longer reproducible too. Therefore, my research questions with which, I set out to explore were as follows:

1. How do the compensation structures of promoter CEOs differ from those of professional CEOs in Indian listed companies?
2. What is the level and impact of performance linked incentives on the compensation of promoter versus professional executives?
3. How does the pay of promoter executives compare to that of professional executives in its relationship to performance?

7. Data and Data sources

Data of top 500 listed companies by market capitalization from India's National Stock Exchange (NSE) was used for this study. The sample dataset covered a 7-year data (i.e. from FY2012-13 to FY 2019-20). Directors' compensation data was sourced from Indian Boards (NSE Prime Database). Firm, governance and market data points were collated from the Prowess database, maintained by the Center for Monitoring of Indian Economy (CMIE) as well as S&P Capital IQ. Annual reports filed by the public companies were used to cross-reference and validate the databases, and populate missing data elements from the databases.

8. Descriptive Statistics

8.1 Sample data distribution

Table -S1 : Sample firm distribution by Industry / Sector

Sector	*# firms*	*%*
Financial	81	16%
Cons Durable	15	3%
Healthcare	50	10%
Construction	48	10%
Services	51	10%
Textiles	12	2%
Diversified	6	1%
Communication	10	2%
Energy	27	5%
Engineering	38	8%
FMCG	44	9%
Metals	25	5%
Chemicals	45	9%
Technology	19	4%
Automobile	29	6%
	500	**100%**

Table -S2 : Sample firm distribution by ownership entity

Entity Type	*# firms*	*%*
Public Sector Enterprise	47	9%
Public Sector Bank	12	2%
Belong to a Business Group	166	33%
Others	***275***	55%
	500	**100%**

8.2 Director Composition on the Boards

8.2.1 Executive vs. Non-Executive vs. Independent Directors

The data sample herein included a total of 25,376 director compensation observations over a 7-year period, including both executive as well as non-executive directors. Of the total observations, executive directors represented 30%, while 70% observations were related to non-executive directors. Each year contributed to about 13-16% of the total data sample. Sample data points corresponding to directors, whose compensation information was not available from the annual reports were excluded from the sample.

Table-A1 : Sample Data set of Directors

FY	*Executive Directors*	*Non-Executive Non-Independent Directors*	*Independent Directors*	*Total Directors*	*Independent Directors %*
2012-13	1123	422	1758	**3303**	***53%***
2013-14	1029	559	1699	**3287**	***52%***
2014-15	1005	571	1801	**3377**	***53%***
2015-16	1043	651	1874	**3568**	***53%***
2016-17	1058	661	2007	**3726**	***54%***
2017-18	1107	700	2169	**3976**	***55%***
2018-19	1164	704	2271	**4139**	***55%***
Total	***7529***	4268	***13579***	***25376***	
Sample %	***30%***	***16%***	***54%***		

Over the 7-year period between 2012 to 2019, proportion of independent directors saw a small, but an increasing trend from 53% to 55%. Notably, this is consistent with the directives laid out by the 2013 Act pertaining to board composition. In fact, the Act requires that for all listed companies, at least one-third of the total number of directors should be independent directors, and the non-executive chairman of the board should be a promoter of the company or related to the promoter. The need for increasing the number of independent directors has been driven by the guidelines that require a majority of the audit committee should be constituted by independent directors.

Table-A2 : Executive vs. Non-Executive Director composition

FY	*Executive Directors %*	*Non-Executive Directors %*	*Independent Directors %*
2012-13	34%	66%	*53%*
2013-14	31%	69%	*52%*
2014-15	30%	70%	*53%*
2015-16	29%	71%	*53%*
2016-17	28%	72%	*54%*
2017-18	28%	72%	*55%*
2018-19	**28%**	**72%**	***55%***

8.2.2 Promoter vs. Non-Promoter Directors

Table-A3 shows a gradual but uni-directional shift in board composition with promoter vs. non-promoter directors. Promoter director representation on the board saw gradual reduction from 24% in 2012 down to 18% in 2019; while during the same time period, Non-promoter director representation increased from 76% to 82%. This trend has been guided by multiple factors, such as the board composition norms of the companies act, along with SEBI's guidelines, including but not limited to the diversity requirements on boards, and proportion of independent directors, among others.

Table-A3 : Promoter vs. Non-Promoter Director composition

FY	*Promoter*	*Non-Promoter*	*Total*	*Promoter %*	*Non-Promoter %*
2012-13	782	2521	***3303***	24%	76%
2013-14	786	2501	***3287***	24%	76%
2014-15	777	2600	***3377***	23%	77%
2015-16	743	2825	***3568***	21%	79%
2016-17	736	2990	***3726***	20%	80%
2017-18	763	3213	***3976***	19%	81%
2018-19	759	3380	***4139***	18%	82%
Total	***5346***	***20030***	***25376***		

8.2.3 Promoter vs. Non-Promoter Executives (Directors)

This trend is also indicative of increased representation of professionals in both executive as well as non-executive board positions. In 2012 for instance, 49% of the executive board positions were occupied by promoter managers; it gradually decreased to 40% in 2019, while professional manager representation on the board steadily increased from 51% to 60% during the same time period.

Table-A4 : Promoter vs. Non-Promoter Executives (Directors)

FY	*Promoter Executives*	*Non-Promoter Executives*	*Total Executives*	*Promoter Executives %*	*Non-Promoter Executives %*
2012-13	548	575	***1123***	49%	51%
2013-14	489	540	***1029***	48%	52%
2014-15	461	544	***1005***	46%	54%
2015-16	460	583	***1043***	44%	56%
2016-17	448	610	***1058***	42%	58%
2017-18	469	638	***1107***	42%	58%

2018-19	470	694	***1164***	40%	60%
	3345	***4184***	***7529***		

8.2.4 Promoters’ role in executive vs non-executive director positions

While there is a clear trend towards attracting professional and independent talent to the boards, as may be noted from Table-A5, a vast majority of promoters still occupied executive positions. In fact, 63% of promoters have been in executive positions, with 37% taking on non-executive positions on the board. This suggests that most firms are not only promoter controlled but are also promoter managed.

Table-A5 : Executive vs. Non-Executive Promoters (Directors)

FY	*Promoter Executives*	*Promoter Non-Executives*	*Total Promoter*	*Promoter Executives %*	*Promoter Non-Executives %*
2012-13	548	234	***782***	70%	30%
2013-14	489	297	***786***	62%	38%
2014-15	461	316	***777***	59%	41%
2015-16	460	283	***743***	62%	38%
2016-17	448	288	***736***	61%	39%
2017-18	469	294	***763***	61%	39%
2018-19	470	289	***759***	62%	38%
	3345	***2001***	***5346***		

8.2.5 Promoter vs. non-promoter CEOs

Table-A6 summarizes the distribution of promoter vs. non promoter CEOs. Over the 7 years of the study period, there is a directional move towards increased professionalization of firms with promoters occupying the CEO role trending down from 57% to 50%. Non-promoter professional executives’ share of CEO roles steadily increased from 43% towards 50%. Notably, this trend has been driven by several evolving factors of growth, including global expansion of Indian businesses, increased institutional investor participation in governance, emerging technological innovations driving the need for hiring and empowering professional talent with specialized / global skills to run the firms.

Table-A6 : Promoter vs. Non-Promoter CEOs

FY	Promoter CEO	Non-Promoter CEO	Total CEO	Promoter CEO %	Non-Promoter CEO %
2012-13	233	179	***412***	57%	43%
2013-14	244	178	***422***	58%	42%
2014-15	238	199	***437***	54%	46%
2015-16	247	218	***465***	53%	47%
2016-17	244	233	***477***	51%	49%
2017-18	257	239	***496***	52%	48%
2018-19	258	253	***511***	50%	50%
	1721	***1499***	***3220***		

8.3 Director Compensation Trends

Compensation details are expected to be disclosed by the listed companies as part of their annual reports; therefore, the disclosure quality and standardization have been evolving by the year. However, there is no one standard way of representing the compensation data consistently across all firms. For example: while some firms presented a detailed breakdown of the compensation against specifically named heads (i.e. salary, perquisites, commission, contribution to PF, performance-linked long-term component, etc.), some other firms represented variable pay as part of the bonus component, while still others represented it as a performance incentive.

Furthermore, some firms included perquisites and other benefits under salary, while others represented it as a separate line item. For the sake of consistency for our analysis, I identify some of the top-level categories for capturing information related to compensation. They include:

- Salary and perquisites
- Commission
- Sitting Fees
- Other Compensation
- Total compensation

For executive directors, most part of the total compensation comprised the salary, along with the commission components. For non-executive directors, in addition to the sitting fees, commission represented a major portion of their net compensation. Herein, it may be noted that independent directors are normally compensated with a combination of sitting fees and commission. Moreover, while the companies act allows firms to pay the sitting fees to executive directors, it is not a common practice to pay the sitting fees to executive members.

8.3.1 Compensation structure and composition

As shown in Tables-B1 & B2 with the mean salary levels broken down by key components, most executive directors' compensation comprised fixed salary and commission. While the fixed portion has been about 70%, commission constituted 30% of the total compensation. For non-executive directors, commission represented the biggest component, while the fixed salary and sitting fees represented 10-15% each. For independent directors, although the companies act allows the payment of salary and incentive components, it is uncommon for companies to use these mechanisms to compensate independent directors. As depicted in Table 2.3 below, close to 75% of compensation of independent directors has been paid as commission, while the rest is paid via sitting fees.

Table-B1 : Compensation components of Executive Directors

(Mean compensation in Lakhs)

FY	***2012-13***	***2013-14***	***2014-15***	***2015-16***	***2016-17***	***2017-18***	***2018-19***	***%***
Sample Size	1123	1029	1005	1043	1058	1107	1164	
Salary	160.02	185.78	226.42	262.73	290.3	325.66	315.94	69%
Sitting Fees	0.13	0.05	0.04	0.09	0.03	0.05	0.05	0%
Commission	67.16	86.1	96.31	111.69	114.78	114.73	140.81	29%
Other	2.74	0.52	0.18	0.09	14.86	24.98	23.08	3%
Total Compensation	***230.06***	***272.45***	***322.96***	***374.6***	***419.97***	***465.42***	***479.89***	

Table-B2 : Compensation components of Non-Executive Directors

(Mean compensation in Lakhs)

FY	***2012-13***	***2013-14***	***2014-15***	***2015-16***	***2016-17***	***2017-18***	***2018-19***	***%***
Sample Size	2180	2258	2372	2525	2668	2869	2975	
Salary	1.27	1.68	0.49	1.88	2.78	5.47	3.05	11%
Sitting Fees	1.47	1.54	3.03	3.74	4.18	4.55	4.98	16%
Commission	9.97	11.86	13.01	14.75	18.24	18.74	17.55	70%
Other	0.05	0.04	0.25	0.3	0.85	3.12	0.66	4%
Total Compensation	**12.77**	**15.12**	**16.77**	**20.67**	**26.05**	**31.88**	**26.24**	

Table-B3 : Compensation components of Independent Directors

(Mean compensation in Lakhs)

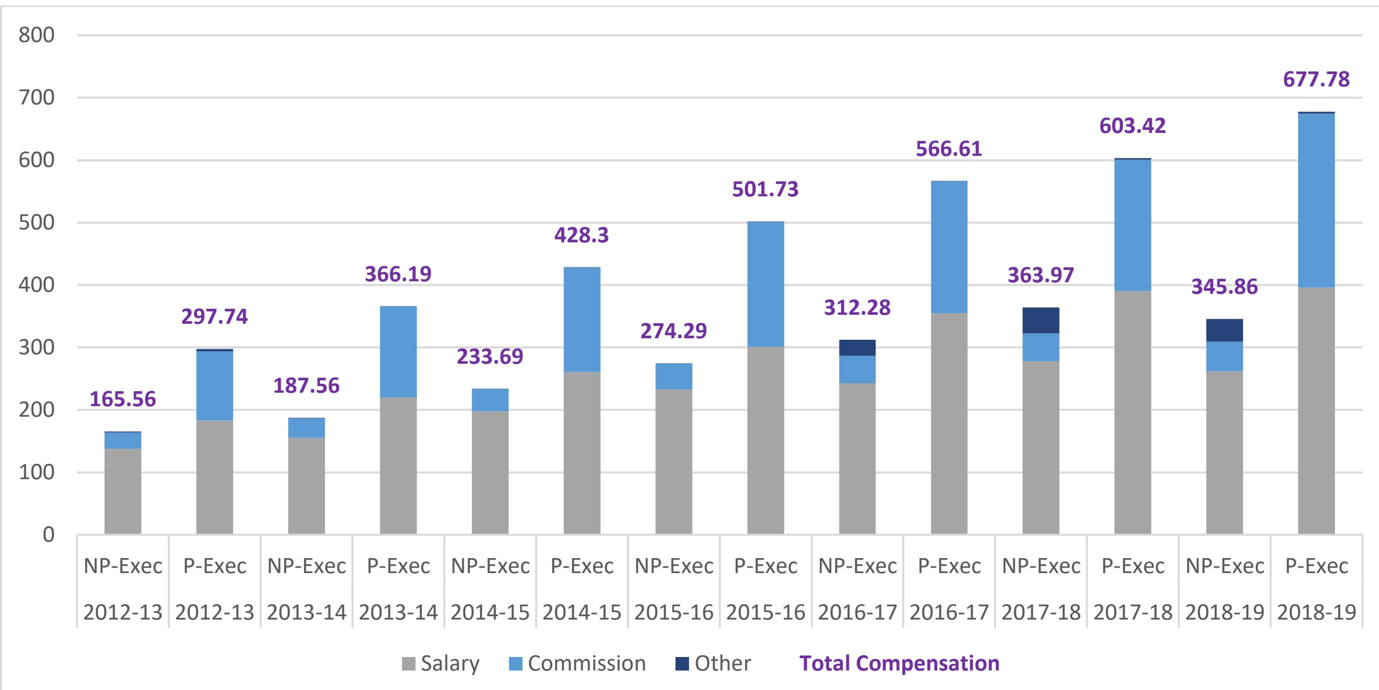
FY	***2012-13***	***2013-14***	***2014-15***	***2015-16***	***2016-17***	***2017-18***	***2018-19***	***%***
Sample Size	1758	1699	1801	1874	2007	2169	2271	
Salary	0.01	0.01	0.08	0.01	0.05	0.14	0.08	0%
Sitting Fees	1.57	1.66	3.37	4.19	4.76	5.16	5.59	27%
Commission	6.73	7.83	9.64	10.62	11.3	11.59	11.69	71%
Other	0.05	0.05	0.14	0.21	0.2	0.18	0.29	1%
Total Compensation	**8.36**	**9.56**	**13.23**	**15.04**	**16.32**	**17.07**	**17.65**	

Further, it is to be noted that from a theoretical perspective of executive compensation design, as described by the Agency theory, the compensation for executives, or at least a major portion of it needs to be aligned to performance-linked portions. Data of the 7-year study period (Table-B1) show that close to 70% of the executive's compensation has been 'fixed' with no direct dependence on performance related outcomes of the firm.

8.3.2 Executive Directors – compensation structure

Sample data of NSE 500 companies over the 7-year period consistently shows a clear trend that the compensation levels of promoter executives are anywhere between 80-100% more than their non-promoter counterparts. As shown in Table B5, participation and representation of non-executive directors on the board shows an increasing trend; interestingly herein, the compensation level pattern has not seen much of change within this time period. This observation in turn, is in line with the hypothesis that promoter managers do enjoy higher privileges relating to compensation in Indian listed firms.

Table-B4 : Promoter vs Non-Promoter Executive Director Compensation Trends (Mean compensation in Lakhs)

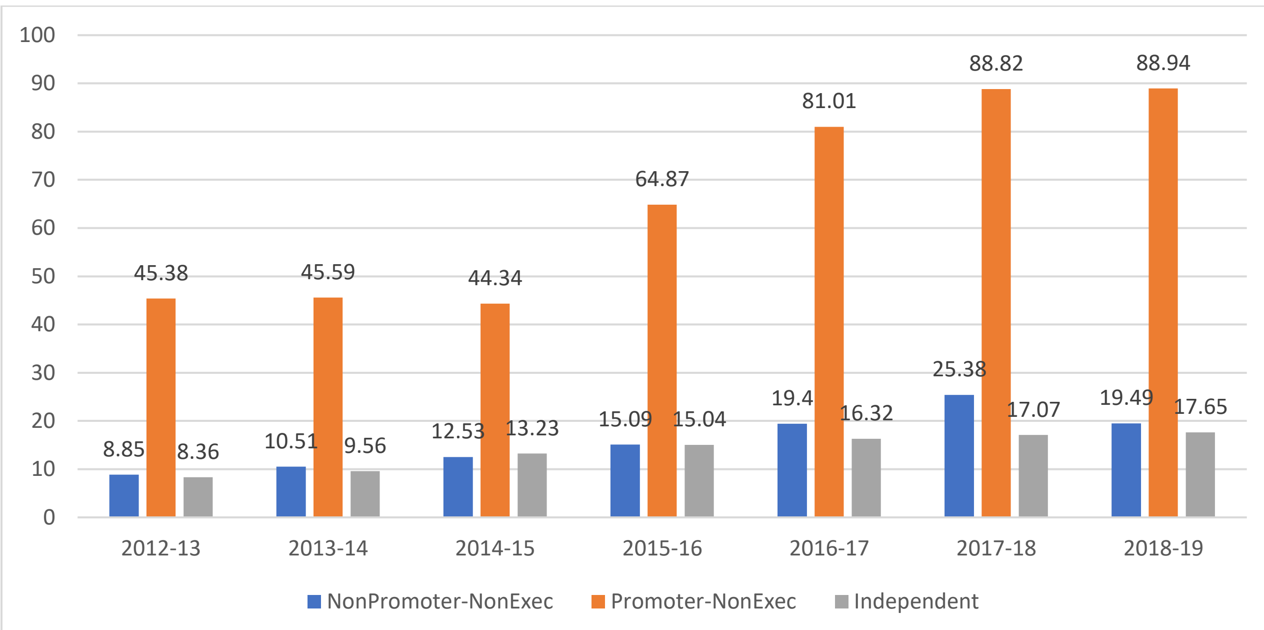


8.3.3 Non-executive directors – compensation structure

In case of non-executive directors, the gap between promoter and non-promoter counterparts is even more pronounced. Non-promoter non-executive directors receive a quarter of the compensation of the non-executive directors from the promoter group. This trend provides an initial indication that irrespective of a director's participation in executive or non-executive capacity, if s/he hails from the promoter group, there is a higher premium attached to the compensation. However, the compensation of independent directors are in line with that of the overall non-promoter non-executive population.

Table-B5 : Promoter vs. non-promoter non-executive director compensation trends

(Mean compensation in Lakhs)



8.3.4 Promoter vs. non-promoter CEO – compensation structure

When it comes to managing directors or CEOs, promoter CEOs take away on average about 50% higher total compensation to their professional counterparts. However, there is a major difference in the composition of the total salary of promoter and professional CEOs. On average, about 60% of promoter CEOs compensation is fixed, and 40% is composed of commission. For non-promoter CEOs, close to 80% of the total compensation is composed of a fixed component (i.e. salary and perquisites), and about 15-20% is represented by commission (Table-B6). This could be indicative of many possible explanations that need to be investigated in more detail. One such possible explanation is that promoter CEOs are compensated through the commission being a relatively short-term realization tool linked to performance goals over a shorter time window, while the professional CEOs being compensated through the long-term performance incentive programs (e.g. stock options) that vest over a long period of time. In fact, stock related option compensation details are not consistently disclosed as part of the annual report, making it thereby difficult to baseline and compare all firms' data uniformly.

Table-B5 : Promoter vs. non-promoter CEO compensation trends

(Mean compensation in Lakhs)

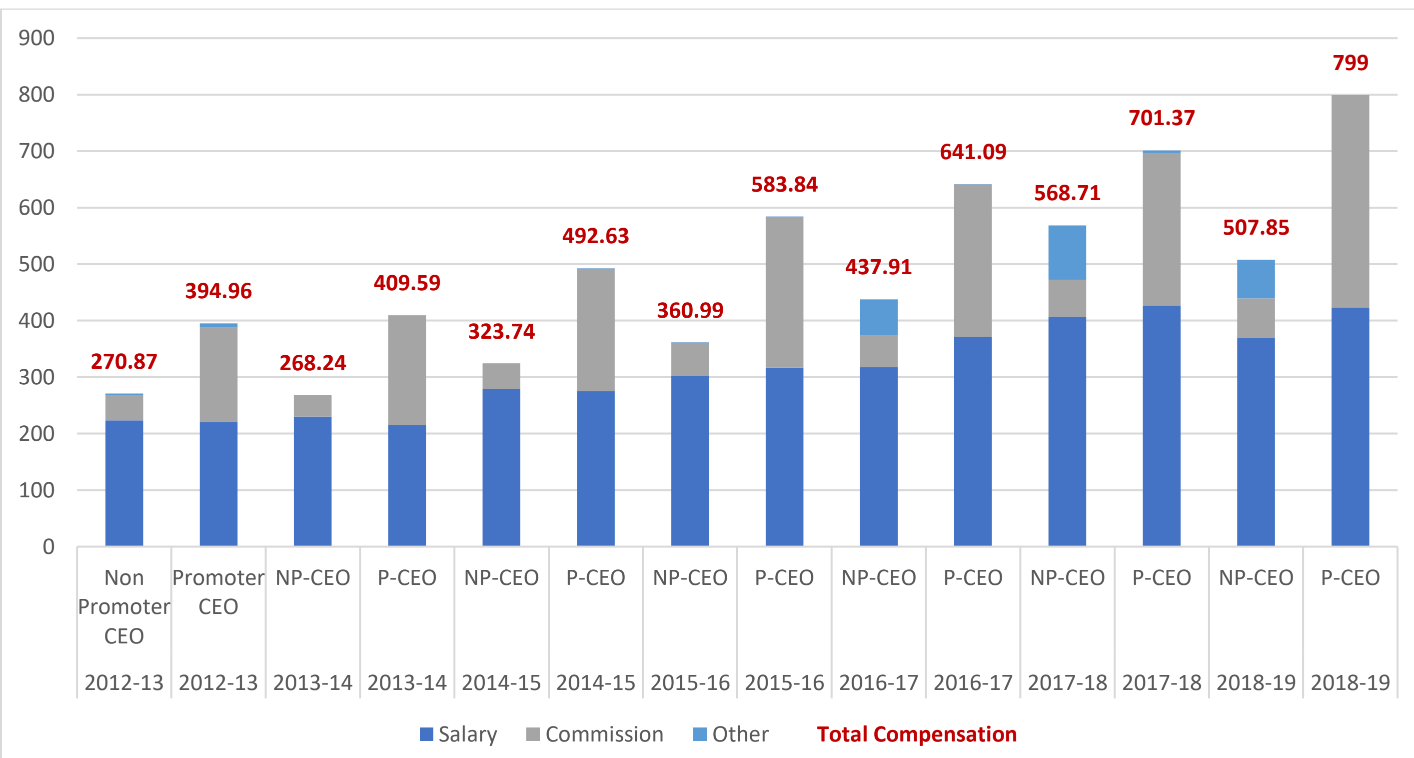
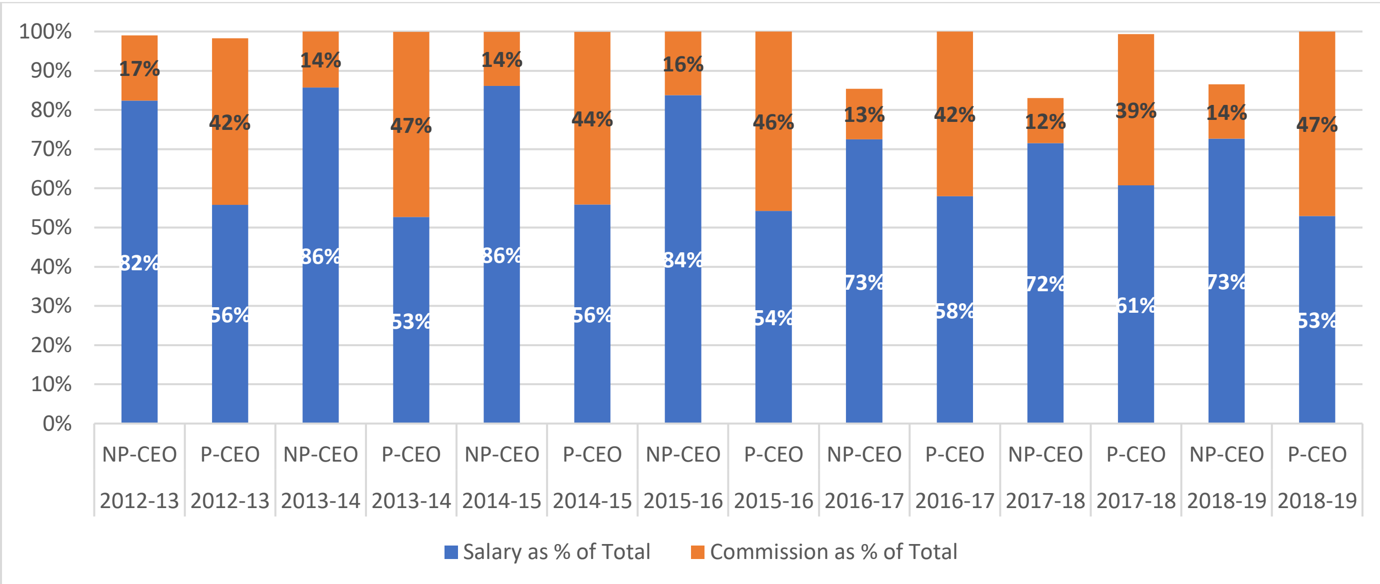


Table-B6 : Promoter vs. non-promoter CEO compensation components

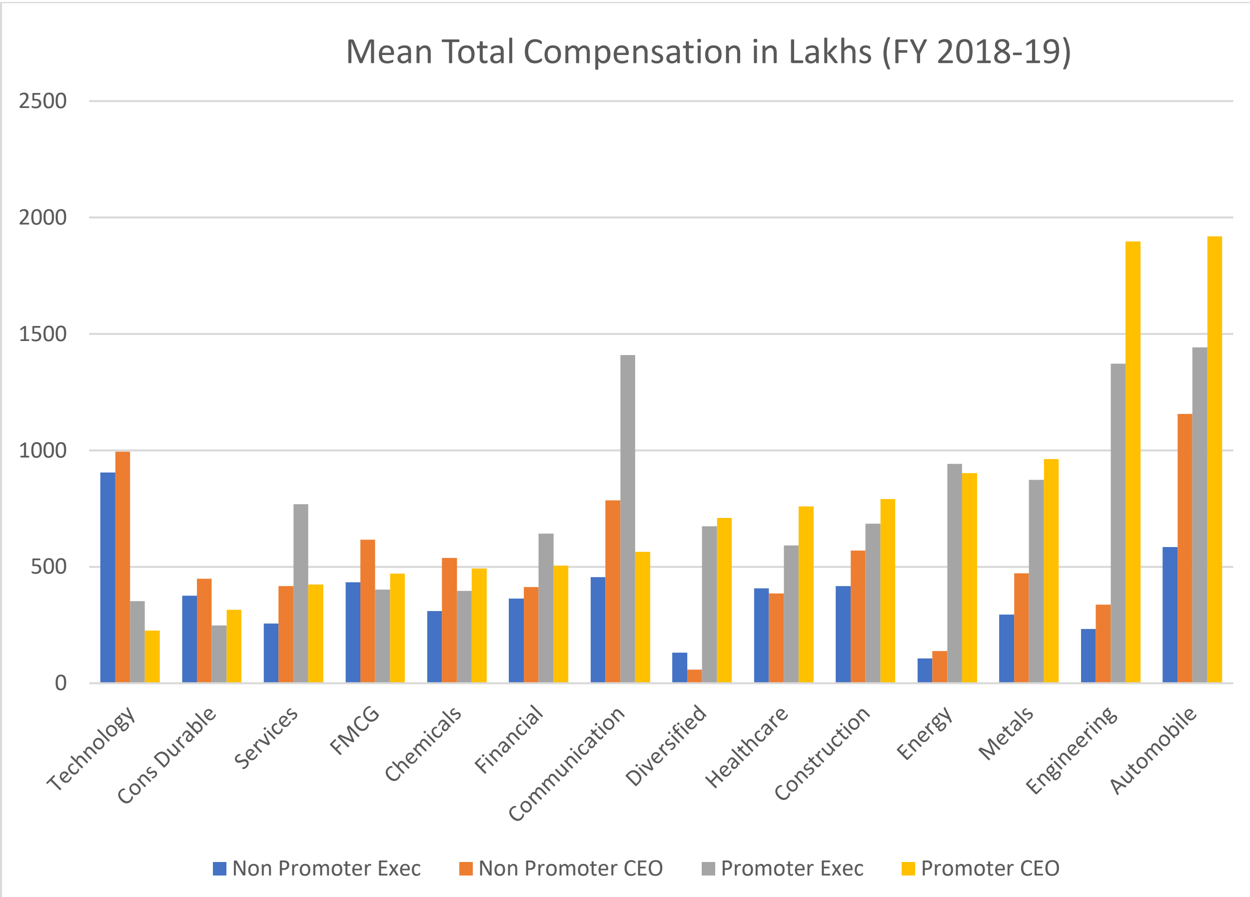
(Mean compensation in Lakhs)



8.3.5 Compensation trends by industry / sector

Across all the sectors of the industry, promoter CEOs predominantly are the topmost compensated category, followed by promoter executives, non-promoter CEOs, and non-promoter executives. Traditional manufacturing and large-scale industries, such as automobile, engineering, metals, and energy are on leading end of the compensation curve, with promoter CEOs and promoter executives being the topmost paid category. An exception to this trend is seen in the technology sector, where non-promoter CEOs and non-promoter executives represent the topmost compensated category. The reason for this is evident in the fact that the technology industry is fast evolving, and the leadership positions need to be sourced from the global talent pool of professionals bringing specialized skills in emerging technologies.

Table-B7 : Sector-wise compensation trends



8.4 Compensation as a function of financial metrics

8.4.1 Guidance from Companies Act 2013

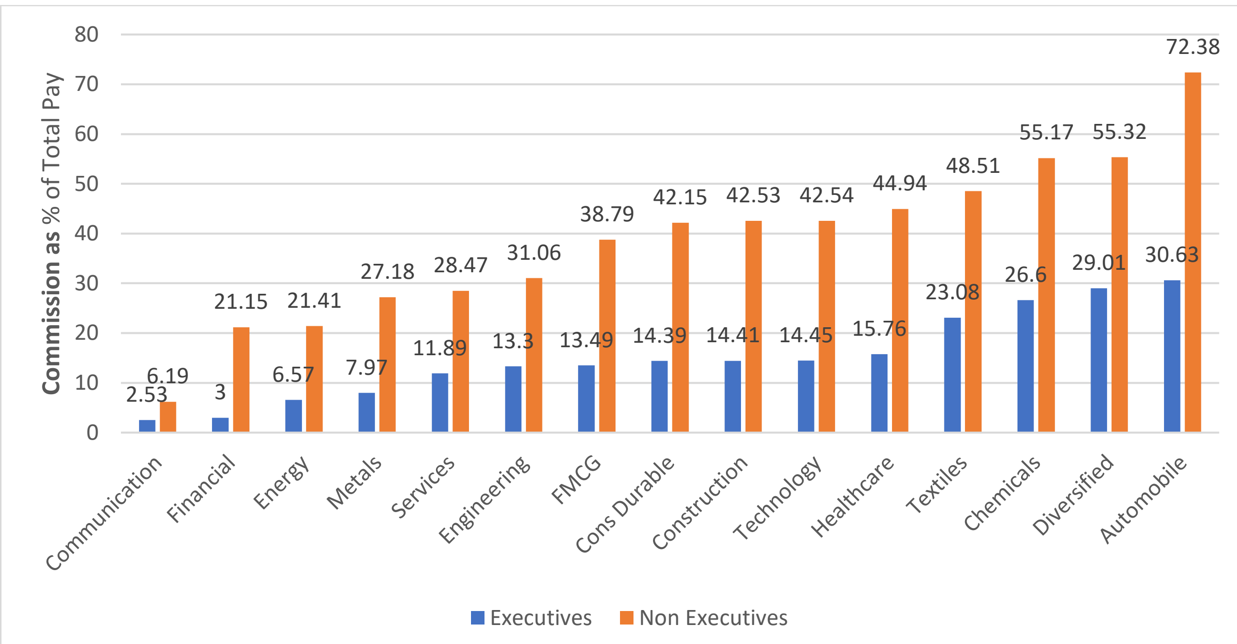
Sections 197 and 198 of the Companies Act 2013 defines the structure and guidelines of managerial remuneration payable by a public company. The total remuneration paid to a firm's directors, including the managing director and whole-time director, as well as its managers in respect of any financial year shall not exceed eleven per cent of the net profits of that firm for that financial year, as computed in the manner laid down in section 198.

As for the structure of the compensation, as shown in section 8.2.1 above, commission is a component that is directly linked to the firm's performance, while most other elements are fixed in nature. Further, as explained by the annual reports of firms, most companies define their commission component as a function of the net profits of the company. This is to ensure that the agent's compensation is tightly linked to the performance, and hence, the outcome value added to the principal to create a closer alignment between the principal and the agents. To examine the linkage between pay and performance, it is essential to closely examine the trends demonstrated in the commission component of the directors in relation to the performance metrics of the company, including but not limited to net profits.

8.4.2 Level of commission for director categories

An analysis of commission as a percentage of total pay received by directors reveals an interesting pattern that could be somewhat counterintuitive. One would expect that going by the spirit of the agency theory, in order to align the interests of executive directors with that of the principals, the commission component plays an important role, as it is determined by the net profits or other related performance factors. Hence, higher the performance-linked commission component, higher would be the pay performance alignment. Notably, executive directors hold positions that are more directly linked to the drivers of a firm's operational performance as compared to non-executive directors, who do not directly participate in execution related processes of the firm. Hence, the representation of the commission as a component of total pay is expected to be higher for executive directors as compared to their non-executive counterparts. Table-C1 shows that during the FY 2018-19 as a sample data point (which is in line with the other years as well) that executive directors' commission represents approximately 15% of their total pay; whereas, for non-executive directors, it is close to 40% on average. This pattern however, could be possible because non-executive directors can only be compensated using sitting fees or commission.

Table-C1 : Commission as a % of total pay (FY 2018-19) by sector



Same analysis extended to each sector of NSE500 companies reveals a stark contrast of the relative significance of commission component for directors in that sector. For instance, firms belonging to the communication and financial sectors have negligible part of the compensation structured as a performance-linked commission. More specifically, the financial sector sample consisted of 58 firms (mostly banks); only 2 of them have any commission as part of the total pay. 56 financial firms paid their executive directors 100% fixed salary with zero commission component. This pattern is consistent with the observations made by the Reserve Bank of India and subsequent guidelines published in November 2019 on the need to balance the fixed pay and the variable pay proportions to better align the director's interest with other stakeholders. The following excerpt from the RBI guideline document outlines that a substantial part (at least 50%) of the total pay needs to be variable pay component that is linked with the firm performance metrics.

> ***(b) Limit on Variable Pay:***
>
> *(i) It should be ensured that there is a proper balance between fixed pay and variable pay. In accordance with FSB Implementation Standards, read with paragraph 2.1.2(b)(iv) and bullet (a) of BCBS stipulations furnished in Appendix 2, a substantial proportion of compensation i.e., at least 50%, should be variable and paid on the basis of individual, business-unit and firm-wide measures that adequately measure performance, except in cases mentioned in paragraph 2.1.2(b)(iii) and paragraph 2.2 of these Guidelines. At higher levels of responsibility, the proportion of variable pay should be higher. The total variable pay shall be limited to a maximum of 300% of the fixed pay (for the relative performance measurement period).*
>
> *(ii) In case variable pay is up to 200% of the fixed pay, a minimum of 50% of the variable pay; and in case variable pay is above 200%, a minimum of 67% of the variable pay should be via non-cash instruments.*

8.4.3 Commission component – promoter vs. non-promoter directors

Tables-C2 and C3 present the commission component as a percentage of total pay for promoter vs. non-promoter executives and CEOs. It is to be noted that the commission component is significantly larger for promoters relative to non-promoters. In fact, the commission on average represents about 27 percent of total pay for promoters; while it is only 7% for non-promoters. Automobiles, chemicals, and consumer durables sectors are on a higher end with an average of 15-17% as commission component. However, the only exception to this trend for overall executives as well as specifically for CEOs is the technology sector, whereby professional CEOs have a 20-25% of the total pay mapped as commission. This is consistent with previous observations made in the earlier section, where it has been noted that the technology sector is also exception, with the total pay level being higher for professional CEOs as compared to promoter CEOs.

Table-C2 : Commission as a % of Total Pay (FY 2018-19)

Promoter vs. Non-Promoter Executives (Directors)

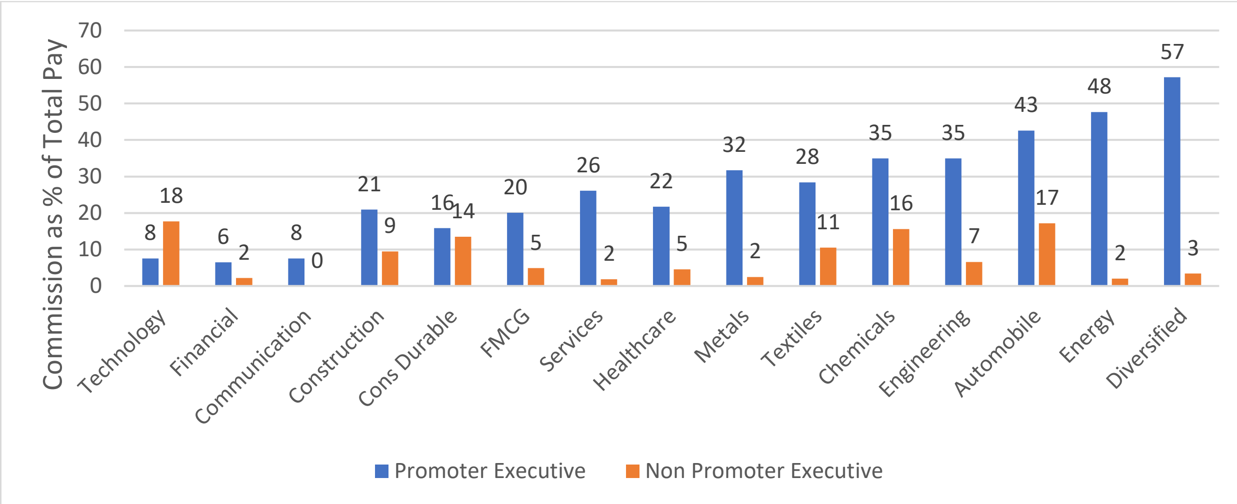
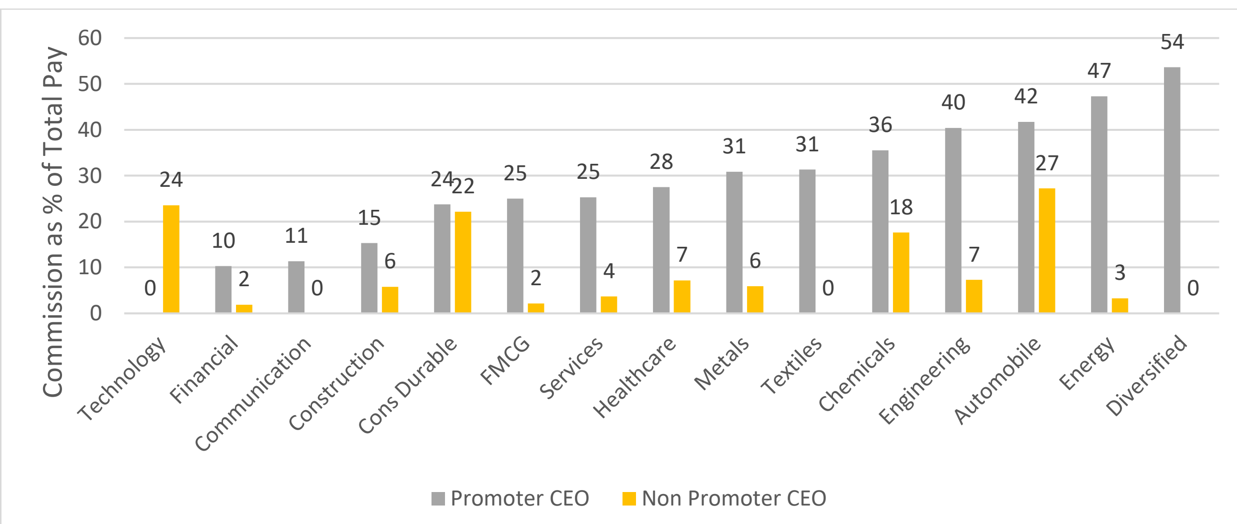


Table-C3 : Commission as a % of Total Pay (FY 2018-19)

Promoter vs. Non-Promoter CEO

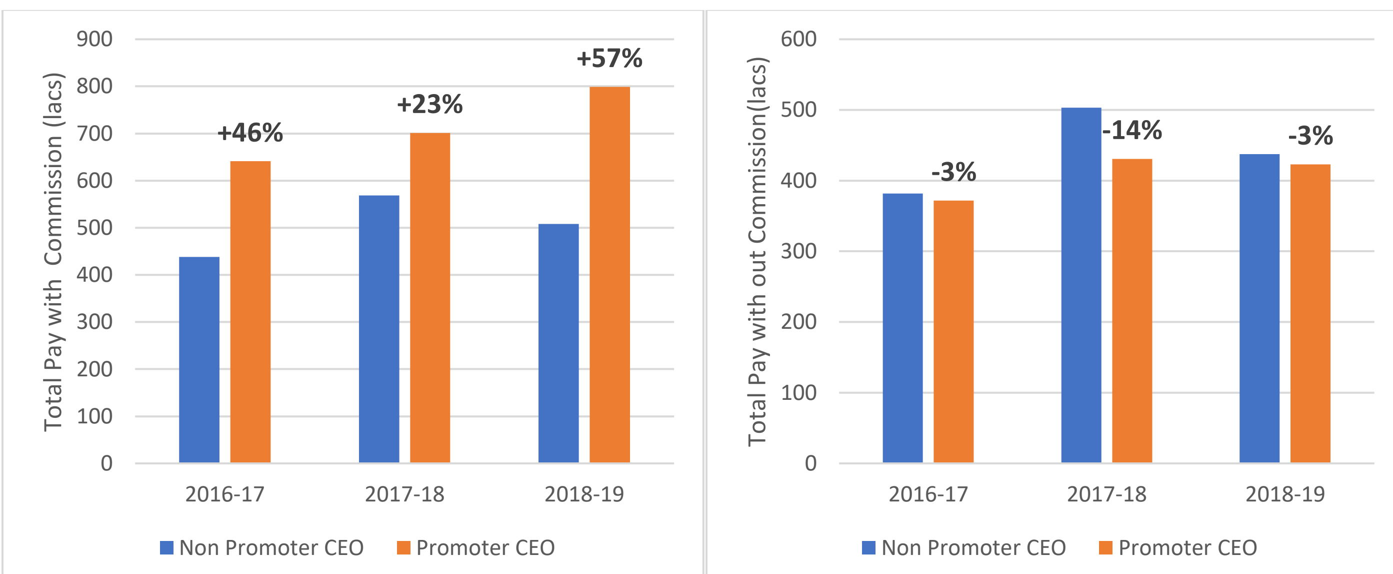


8.4.4 Fixed pay comparison – promoter vs. non-promoter directors

From section 8.2.2 it is clear that there is an identifiable difference in the pay levels of promoter and non-promoter executives. Section 8.3.3 clearly outlines that the commission component is a big differentiating factor between promoters and non-promoters' total pay structure. Taking the commission component away from the total pay, Table-C4 (below) covers a salary comparison of promoter and non-promoter CEOs, both with and without considering the commission component.

Table-C4 : Pay 'with & without' commission

Promoter vs. non-promoter CEO



Both these charts show that while the total pay level is higher for promoter CEOs, most of this premium can be attributed to commission alone. Without commission, the pay levels of promoter vs. non-promoters appear to be comparable. This in turn, gives rise to some further questions that need to be probed on the factors and the reasons that explain a firm's decision to exclude commission as a performance-based compensation component for non-promoter CEOs.

9. Key Variables – pay, performance and others

9.1 Pay

CEO Pay is taken as the natural logarithm of the 'total compensation' as disclosed by companies. Some firms present a detailed breakdown of the compensation against specifically named heads, such as salary, perquisites, commission, contribution to PF, performance linked long-term component, etc. Some firms on the other hand, represent variable pay as part of the bonus component, while still others represent it as a performance incentive. Furthermore, while some firms include perquisites and other benefits under salary, others represent it as a separate line item. For the sake of consistency for this analysis, I identify the following top-level categories as variables as the contributing components of 'total compensation'. For instance, all stock compensations, such as stock options are shown under the 'other compensation' variable at the time of exercising as final realized proceeds of the sale of such grants.

- Salary and perquisites
- Commission
- Sitting Fees
- Other Compensation

9.2 Performance

Consistent with global studies investigating the pay-performance linkage, I used Return on Assets (ROA) as the base measure indicator of the accounting performance of a firm. Further, I calculated the concept of 'industry adjusted firm performance' by subtracting a given firm's performance (ROA) in a year from the industry peer group's median ROA of the same financial year. Industry peer group is identified using the 3-digit NIC code of firms, as published on the National Stock Exchange. Thereby, industry adjusted ROA shows the 'excess performance' delivered by a given firm relative to the median of its industry peer group.

9.3 Variable description

Description	Variable Name	Definition
Compensation variables		
Salary	Salarylacs, lsal	Salary component / fixed cash part of total compensation paid in an accounting year & Log(Sal)
Commission	Commissionlacs, lcom	Bonus / commission part of the compensation. Generally defined as a component linked to performance goals & Log(commission)
Stock compensation	Otherlacs	Stock grant / stock options-based compensation
Total compensation	Totalcomplacs, ltotcomp	Total Compensation paid in an accounting year & Log(comp)
Governance variables		
Board size	boardsize	Board Size : Numbers of directors on the board
Family In Board	Promo_brd_pct	% of promoter family members on the board
Independent directors	indep_board_pct	% of of independent directors on the board
Firm Variables		
Size of the Firm	firmsize	firmsize = log(assets)
Age of the Firm	Firmage	Years of establishment
Industry	Sector	Sector / Industry the firm belongs to
Market Risk	beta	Risk measured with market volatility
Family firm	Promoter	Is this a promoter owned / family-owned firm?
Industry classification	Nic	3-digit Industry category classification (National Industrial Classification)
CEO variables		
CEO Tenure	Tenure	Number of years CEO is employed with the firm
CEO age	Age	CEO Age
CEO Board Chair	dual	Whether or not CEO is also chairperson of the board
Promoter CEO	p_md	Is the CEO from the promoter family?

Performance variables		
Sales	Sales, lsales	Annual sales of the firm in an accounting year & Log(sales)
Return on assets (in %)	Roa	Ratio of earnings before interest and taxes to total asset
Return on Capital (%)	Roc	Return on Capital (%)
Revenue	revenuecr, lrev	Annual revenue of the firm in an accounting year (in Crores) & log(revenue)
PAT	Patcr, lpat	Profit after tax in an accounting year (in Crores) & log(PAT)
Market Cap	MktCapCr, lmktcap	Market capitalization of the firm (in Crores) & log(MarketCap)
Industry adjusted performance	roa_dif_med	Industry adjusted ROA = ROA – Median of ROA of industry peer group for that year
Ownership Variables		
Ownership Type	entitytype	Indian Promoter, Foreign promoter, Public, Government, Institutional
Promoter ownership	promo_pct	% of shares held by promoters
Institutional ownership	inst_pct	% of shares held by Institutional shareholders

10. Research Methodology and Design

From the data collected, I looked to construct a panel data as the source for all further analysis, while aiming to delve deeper into probing questions on the pay levels of promoter managers vis a vis their professional counterparts relative to the performance of firms delivered under their stewardship. In the process, I removed some firms from the base data of the top 500 NSE listed firms by market capitalization to create a relevant base dataset for this analysis. Specifically, at first, I removed government firms (60) from the base data, as they are government controlled (e.g. ONGC, IRCTC etc.), owing to which, the nomination and remuneration of CEOs follow a very different approach as determined by the Indian government as the promoter.

Then, I classified the remaining firms into industry groups, using the standard NIC classification that is used by the Indian industry, and is available on the National Stock Exchange's website. Notably, NIC or the National Industrial Classification helps create peer groups of firms with comparable industry classes. My rationale for using this was to calculate the industry adjusted performance (ROA) of a firm.

Table-1 provides a summary statistic of the key variables used in the model and their correlations. From the table, it may be noted that the average CEO compensation is INR 7.59 crore, and the average commission is INR 2.7 crore. From the total sample of 369 firms, excluding PSUs, 209 firms are family managed, while 160 firms are managed by professional CEOs, who do not belong to the promoter family. Further, it may be noted that in promoter-managed firms, promoters hold an average of 50% of outstanding shares, while institutions hold 27.6% of shares on average.

Table-1 reports the basic statistics of the variables used in the model and the correlations amongst them.

		N	Mean	SD	1	2	3	4	5	6	7	8	9
1	totalcomplacs	2011	759.1	1125.5	1								
2	commissionlacs	2011	271.2	696.3	0.67***	1							
3	p_md	2011	0.6	0.5	0.06*	0.18***	1						
4	roa_dif_med	2011	0.01	0.04	0.15***	0.22***	0.03	1					
5	firmage	1936	41.5	23.4	0.02	0.04*	-0.04	-0.11***	1				
6	promo_pct	2011	50.7	18.2	-0.08***	-0.05*	0.19***	0.06**	-0.15***	1			
7	inst_pct	2011	27.6	15.5	0.15***	0.07**	-0.20***	0	0.01	-0.64***	1		
8	promo_board_pct	2011	0.2	0.2	0	0.08***	0.66***	0.04	-0.03	0.28***	-0.25***	1	
9	assetscr	2011	34994	124298	0.19***	0.01	-0.19***	-0.02	-0.01	-0.27***	0.39***	-0.21***	1

*** $p < 0.001$; ** $p < 0.01$; * $p < 0.05$

11. Model - Findings and Discussion

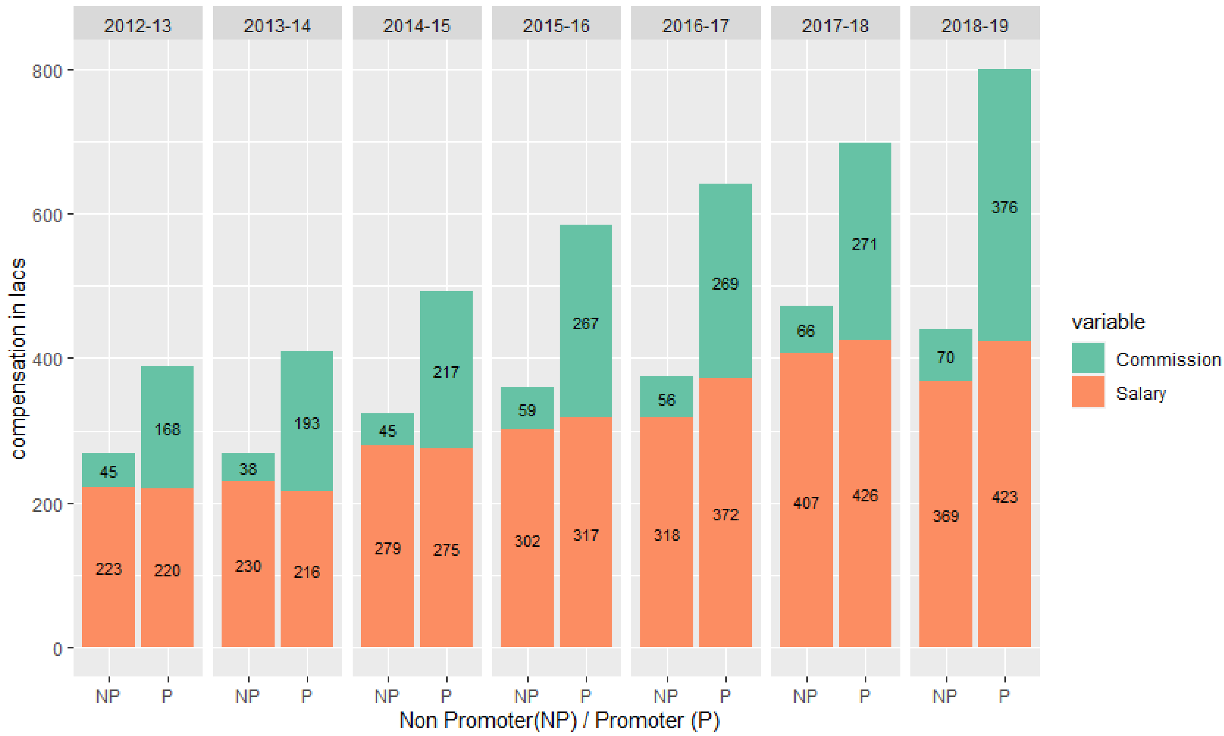
Econometric approaches are applied to examine cross-sectional and time series panel data, using fixed effects modeling techniques for evaluating the impact of various parameters of industry adjusted firm performance on the compensation levels. Herein, 'compensation' is modeled as a dependent variable in the regression model. In fact, I used various components of compensation, such as fixed salary and commission as dependent variable. Further, it may be noted that a firm's annual reports, along with board reports represent and describe the executive compensation as a 'function' of various firm-level parameters as explanatory variables. These variables include firm-specific variables, industry-specific variables, performance variables, governance variables, ownership variables, etc.

Given that my data sample covers both cross-sectional and time-series panel data, I used the fixed effects model to capture the time-specific as well as firm specific intercepts.

$$
\begin{aligned}
&Log(Total\ Compensation_{i,t}) \\
&\quad = \beta 1 * (Performance\ Var_{i,t-1}) + \beta 2 \\
&\quad * (Governance\ Var_{i,t-1}) + \beta 3 * (Firm\ Var_{i,t}) + \beta 4 * (Market\ Var_{i,t}) \\
&\quad + \beta 5 * (Ownership\ Var_{i,t}) + \beta 6 * Industry\ Fixed + \beta 7 * Firm\ Fixed + €
\end{aligned}
$$

$$
\begin{aligned}
&Log(Commission_{i,t}) \\
&\quad = \beta 1 * (Performance\ Var_{i,t-1}) + \beta 2 \\
&\quad * (Governance\ Var_{i,t-1}) + \beta 3 * (Firm\ Var_{i,t}) + \beta 4 * (Market\ Var_{i,t}) \\
&\quad + \beta 5 * (Ownership\ Var_{i,t}) + \beta 6 * Industry\ Fixed + \beta 7 * Firm\ Fixed + €
\end{aligned}
$$

Chart -1 : compensation levels and composition



I observe that under the ‘total salary terms’, promoter CEOs are paid higher than professional CEOs (i.e. almost 30-40% higher when compared at the mean levels). In fact, this observation has also been widely quoted in the media, along with several papers written in the Indian promoter executive compensation literature in support of the managerial power theory, Chen et al(2021) .

Chart-1 shows that the fixed salary component is comparable between two groups, and the commission component is significantly higher, directly contributing in the process to the higher total compensation. Notably, the commission component as defined in the annual reports is established by linking it to performance goals defined for the CEO. It is evident from the chart that a significant portion of non-promoter CEO’s pay is a fixed component relative to promoter CEOs. In fact, about 40-45% of the total pay of promoter CEOs is represented by the commission component. This indicates that the boards/NRCs are able to link a significant portion of the promoter CEO to the 'commission' component of the pay.

This argument gives rise to an important aspect - It is quite possible that the 'commission' is just a label given to a component of the pay, and the term by itself may not be assumed for the existence of a strong relationship between the incentive provided towards performance unless it is tested and proven to be linked to performance. A good performance linked commission component must demonstrate high sensitivity towards the delivered performance with the level of commission and the pay moving in line with firm performance. This test is incorporated into the fixed effects model and the findings from the model are detailed in Table-2.

Table-2 : Firm fixed effects Linear Regression Models on Total compensation

CEO Total Compensation in Log terms

	CEO Pay by Promoter	Pay Performance Sensitivity		Effect of other controls
	(1)	(2)	(3)	(4)
(Intercept)	4.65 (0.18) ***	4.60 (0.17) ***	4.58 (0.17) ***	12.31 (1.90) ***
p_md	0.36 (0.08) ***	0.32 (0.08) ***	0.33 (0.08) ***	0.32 (0.08) ***
roa_dif_med		4.74 (0.53) ***	3.13 (0.98) **	3.05 (1.02) **
p_md:roa_dif_med			2.12 (1.08) *	2.14 (1.11)
firmsize				0.18 (0.09)
firmage				-0.13 (0.02) ***
promo_pct				-0.07 (0.02) **
inst_pct				-0.03 (0.02)
promo_board_pct				0.20 (0.32)
R^2	0.79	0.80	0.80	0.80
Adj. R^2	0.75	0.76	0.76	0.76
Num. obs.	2011	2011	2011	1936

*** p < 0.001; ** p < 0.01; * p < 0.05

Base model (1) shows that a CEO coming from the promoter family has a sizable impact on the CEO total pay with a significant beta of 0.36 indicating that the promoter managers earn 43.3% ($e^{0.36}$-1) more than the professional CEOs.

Model (3) shows that for a 1 standard deviation increase (0.043) in the industry adjusted ROA performance, promoter CEO total compensation increases by 9.5% ($e^{2.12 * 0.043}$-1) more than the professional CEOs.

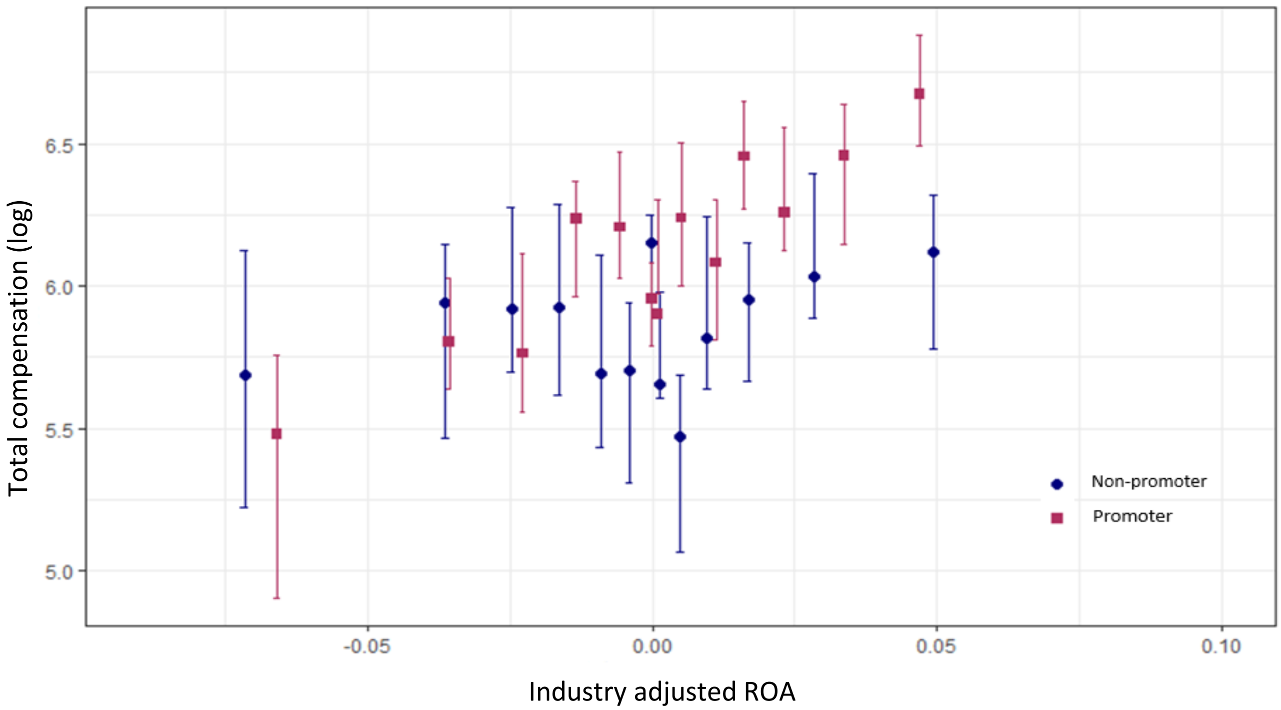
Table-3 : Firm fixed effects Linear Regression Models on commission

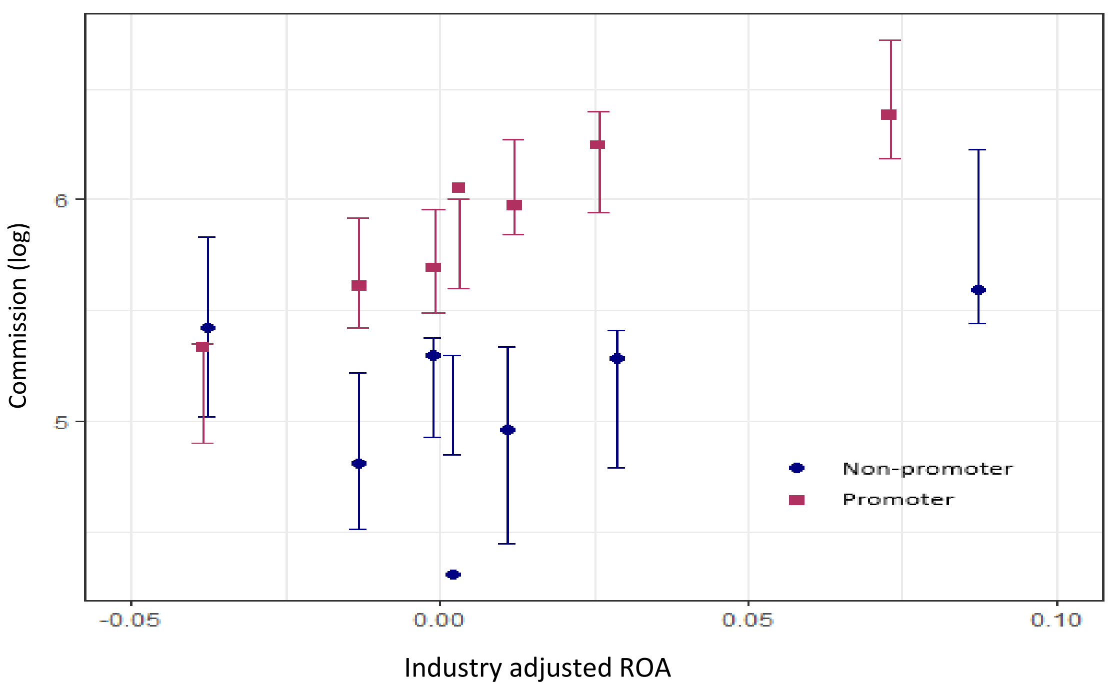
	CEO Commission in Log terms		
	Commission by Promoter	Pay Performance sensitivity	Effect of other controls
	(1)	(2)	(3)
(Intercept)	3.80 (0.21) ***	3.71 (0.21) ***	-2.72 (1.17) *
p_md	0.66 (0.14) ***	0.64 (0.14) ***	0.64 (0.14) ***
roa_dif_med		5.57 (1.18) ***	5.47 (1.24) ***
firmsize			0.36 (0.16) *
firmage			0.02 (0.02)
promo_pct			0.05 (0.02) *
inst_pct			0.04 (0.02) *
promo_board_pct			-0.01 (0.52)
R^2	0.85	0.86	0.86
Adj. R^2	0.80	0.80	0.80
Num. obs.	940	940	900

*** p < 0.001; ** p < 0.01; * p < 0.05

Base model (1) shows that the commission component of Promoter CEO is 93.4% ($e^{0.66}$-1) more than the professional CEOs.

Chart -2 : binned plots from Firm fixed effects regression model





The binned plot above helps in visually examining the relation between industry-adjusted performance of firms to the total compensation and commission of promoter vs. non-promoter CEOs. Importantly, promoter CEOs earn a higher level of compensation when the performance is at the positive end of the industry median, while their compensation is lower than professional CEOs when the performance is lower than the median. This does affirm a higher pay-performance sensitivity for promoter CEOs.

11.1 Test for Pay Asymmetry

Chen et al., (2021) reported that the promoter CEOs' pay was asymmetrically linked to high performing vs. low performing firms. They found that promoter CEOs are paid higher compensation during the years when the firm performance is higher, while on the other hand, they are not paid lower during the low performing years. Effectively, this demonstrates a trend of 'heads I win, tails you lose' when it comes to promoter CEO compensation. To test such scenario, I constructed two variables that differentiate the firm-year observations as high performing and low performing. 'High performing promoter firm' is defined as a firm-year observation having a promoter CEO with the industry adjusted return of the firm in that year, which is higher than the median of the industry peer group in the same year. Similarly, 'low performing promoter firm' is defined as a firm-year observation having a promoter CEO with the industry adjusted return of the firm in that year is lower than the median of the industry peer group in that year.

Table-4 : High vs Low performing Promoter managed firms

	CEO Total compensation in Log terms (A)
(Intercept)	2.18 (0.29) ***
Promoter managed High Performing firm (p_hp)	0.30 (0.08) ***
Promoter managed Low Perfrming firm (p_lp)	0.37 (0.10) ***
Industry adjusted ROA (roa_dif_med)	5.20 (0.80) ***
Size of the firm (firmsize)	0.29 (0.02) ***
Age of the firm (firmage)	-0.00 (0.00)
Institutional holding (inst_pct)	0.01 (0.00) ***
Promoters on the board (promo_board_pct)	0.54 (0.21) *
Promoter managed High Performing firm * Firm performance (p_hp:roa_dif_med)	-1.29 (1.20)
Promoter managed Low Performing firm * Firm performance (p_lp:roa_dif_med)	3.30 (2.32)
R^2	0.20
Adj. R^2	0.19
Num. obs.	1936

*** p < 0.001; ** p < 0.01; * p < 0.05

Model (A) in Table-4 shows that the CEO pay is significantly linked to firm performance; and the linkage is highly sensitive in case of promoter managed firms. It also shows that there is no asymmetry in the treatment of promoter CEO's compensation in the case of high performing or low performing years. This finding does not seem to concur with the findings reported by Chen et al., (2021). This is interesting, because I used the same methodology of testing that scholars in the past used as well. In fact, this disparity in results can possibly be clarified by the differences in the temporal scope of the underlying data. For instance, Chen et al., (2021) examined data from 277 companies listed on BSE's S&P 500 for the years 2004 to 2013, while my dataset encompassed S&P 500 companies from 2013 to 2020. The variation in my findings may be traced back to the successful enforcement of stringent corporate governance reforms that stemmed from the amendment of the Companies Act 2013, along with the incorporation of recommendations from various committees, which led to the formation of multiple regulations. In fact, the implementation of regulations and recommendations has played a crucial role in enhancing the disclosure quality for the purpose of achieving better transparency in terms of executive compensation. Moreover, this effort also led to an increase in the empowerment of independent directors, while reinforcing board independence. By mandating a comprehensive disclosure of executive and key management personnel compensation, as well as providing an explanation of how it is linked to changes in key performance metrics, along with disclosing the ratio of executive compensation to median employee compensation, these measures have effectively helped improve transparency for minority shareholders, as well as institutional investors. Facilitated by enhanced disclosures, proxy advisory firms have substantially increased their involvement in advocating for minority shareholders through providing unbiased recommendations on executive compensation proposals during proxy campaigns. This shift in direction observed through my study relating to the link between pay and performance for incentive-based managers is evidence of the efficacy of developing regulations surrounding the quality of disclosure in annual reports.

12. Comments / Inputs from Industry Experts / Practitioners

In addition to the quantitative examination of the compensation components, and their relationship to firm performance, this study incorporates views of 'practitioners' from the industry in the form of qualitative interviews. The practitioners included board members, CEOs and CHROs of S&P 100 companies, proxy advisors, leading executive compensation consultants, industry experts, as well as proxy advisory firms. Practical insights from them immensely helped in understanding the board room dynamics, competition within the executive leadership talent pool, along with the influence of various practical factors that play an important influential role in determining executive compensation, particularly in promoter-managed firms.

The process I followed to collect the comments of the industry practitioners is as follows - I would introduce myself to the interviewee / industry expert, spend a few minutes of interaction to build the credentials of my research journey and seek their permission to make notes from the interview, and reinforce the aspect of anonymity, while incorporating their comments/inputs into my research work/dissertation. I would then present my research questions, research methodology, data and present the findings of my research. Then, I asked them open-ended questions to justify/validate my findings, and noted any aspects that they felt were surprising, based on their extensive industry or board room experience.

These interviews enhanced my findings in many valuable ways, providing a unique perspective, which is rarely present and beyond the data that can be presented in the annual reports and databases. In other words, these expert interviews presented ‘alternate explanations’ to some aspects that surfaced through the data that I considered as anomalies to the theory, and helped place them in the context of boardroom realities of the industry.

Summary of key inputs / comments from these interviews are listed as follows:

1) Comments from a very senior board member of 10+ listed firms, majority of them being promoter managed, mentioned that s/he is not surprised about the pay-performance sensitivity of promoter-managed firms being higher than professional-managed firms, due to the deep domain and industry knowledge the promoter family executives bring to some of the leading businesses. Such knowledge was considered extremely difficult to find in the market from professional executives outside the family, especially in certain brick-and-mortar and traditional manufacturing businesses.
2) Higher pay in the form of fixed salary or higher commission for promoters is explained partly by the restriction that promoters cannot be issued ESOPs like professional managers, according to the prevailing corporate act, and that there needs to be a compensating control in place. It was

also noted that the next generation of young family members of the promoter family, who are mostly foreign educated, and worked in the professional industry prior to taking on the family business, are increasingly challenging the artificial restriction that is prevailing in India not allowing stock-based compensation for promoter CEOs.

3) In addition to the hard financial factors such as PAT, Revenue goals, ROA and ROCE, a key input that was provided was that boards do consider multiple non-financial goals/factors to assess the accomplishments of the executives, which is not always reflected in the annual reports' compensation analysis section. Examples of such key goal factors include leadership culture, succession planning, L&D impact, productivity etc.
4) A view from the proxy advisory space commented that the finding of a shift towards increased commission component of promoter CEOs from the earlier pattern of base salary being higher is an indication of an easier camouflage for taking away more cash from the company by promoters, under the component, which is technically tied to performance. Besides, I noted that there exists a strong sense of entitlement in the promoter CEO's mind on what s/he deserves to be paid for his/her unique contributions in the role of an executive.
5) Proxy advisory professionals also opined that the disclosures that are mandated today are only restricted towards the pecuniary aspects of the compensation. But promoters do have a pattern of being compensated by the company, using some unique and special benefits and privileges in the form of perks that are well beyond what is paid to professional CEOs. They also opined that the 'excess compensation' of promoters is now

represented by these unique intangible perks. When the regulation of the future mandates disclosures of these benefits, it would clearly bring to the fore the excess element of the compensation of promoter executives. Herein, it may be added that the scope of my dissertation has been limited to formal compensation components that are defined by the Companies Act '2013, and hence the analysis of this element is out of the scope of this research.

6) A board member observed that while there is clearly a sense of entitlement for the promoter family member executives in matters of executive compensation, he noticed an increased awareness of promoters that minority shareholders are watching them, and they need to demonstrate right behaviors in the spirit of corporate governance. Additionally, he opined that the change of trend of promoter pay patterns showing higher sensitivity to performance is an indicator of the changing mindset.

7) Social media and the business media are playing an active role in shaping the thinking processes; and the sense of entitlement of promoter executives, which is becoming an important tool for promoters to manage the market perception, which is directly tied to their firm valuation and stock price. In fact, this was pointed out as a factor influencing the changing landscape of the pay-performance sensitivity of promoters.

8) An interesting comment from an independent director who is on nomination and remuneration committees of a few listed companies was that – earlier, the power came from bringing in capital into the firm, but now, with the changing social dynamics, the power of the promoters and

family members is determined by social influence, market perception management, good governance quotient. These changing social aspects possibly serve as a primary reason for the changing dynamics of executive compensation of promoters.

9) A very senior executive compensation consulting leader commented that the compensation disclosure quality related regulations have not been enhanced in a long time, and it is leaving a lot of scope for the promoter executives and professional CEOs alike to design compensation packages without a need to explain a clear linkage to the performance measures considered for the compensation awards.

10) In the context of comparing the Indian scenario with US-based promoter managed companies, it was observed that boards in the western world are able to demonstrate higher authority compared to boards in India in questioning the executives. Importantly, proxy advisory firms, and the role played by institutional investors is far more active in the western markets.

11) In an emerging market like India, boards are still not able to truly take the serious role of being the representatives of minority shareholders, as the retail shareholders in India are not yet able to engage in intelligent conversations because of lack of any credible data they have access to. Therefore, retail shareholder awareness and education has been observed to be a key determinant of the board's true independence in the emerging world.

12) A senior proxy advisory professional opined that in India, even institutional shareholders are not yet taking an active role in matters of

corporate governance. In such an environment, expecting the retail shareholders to have any meaningful participation in board matters is thereby far-fetched.

13. Contribution of the study

13.1 Contribution to Literature

Several studies in the past have focused on explaining the executive compensation structures and trends from the viewpoint of addressing the classical vertical agency risks from a western corporate perspective. However, the Indian corporate environment has primarily been dominated by the unique phenomenon of promoter family ownership and control, and it introduced an aspect of horizontal agency models.

Moreover, much of the limited literature from Indian context focused on the level of compensation of promoter CEOs, arguing that such a higher level of promoter compensation is an indication of managerial power, and questioned the role of boards and NRCs in controlling the promoters' pay. With my study, I contribute to existing literature by examining the higher levels of promoter pay with the performance delivered by these firms to shareholders at large. I noted that there is a strong relationship, and the correlation between higher pay of promoters to higher performance delivered by them when compared at the industry peer groups, they belong to. Taking this observation forward, I establish that the perception gap that is created between the popular narratives provided by the media in the minds of minority shareholders on this topic reflects poor disclosure quality of executive compensation standards that exist today. Based on my findings and interviews with senior practitioners, I believe that annual reports' disclosures are barely enough to allow a minority shareholder to make an inference, and judge the appropriateness of pay vs. performance when they vote on these proposals. With this, I contribute to existing literature on the need for improved pay disclosures, and the specific performance measures used by the boards to uplift the spirit of corporate governance in the Indian corporate environment, and thereby encourage meaningful participation of minority shareholders in the process of governance.

13.2 Contribution to Practice

We are witnessing a trend of increased participation of minority shareholders in the Indian corporate context, by way of having their say in the form of casting their votes on annual proxy proposals. Institutional investors are now taking an active role in directly participating in aspects of corporate governance of the companies they invested in. Nowadays, we are seeing more institutional investors voting down the executive pay proposals. This increased participation is supported by several enabling controls from SEBI, the Companies Act 2013 as well as the role played by proxy advisory firms. For instance, e-Voting although introduced years ago, has gained greater traction due to the pandemic, and has now become a positive enabler of minority shareholder participation. Secondly, proxy advisory businesses in India have grown from its infancy, and have evolved into an active entity promoting shareholder awareness, particularly in terms of providing analytical insights and recommendations to institutional shareholders. Notably, it is essential for the minority shareholders to have quality disclosure on the compensation structures, the factors that are driving the performance goals of the executives, and how the performance linked variable components are linked to the objective performance metrics established by NRCs of the boards. With this study, I contribute towards lending greater insights backed by facts and analytics in the hands of promoters, board members, wider shareholder base, independent directors, and the NRC to help them analyze the gaps over time, and thereby move towards establishing legitimacy in the compensation design processes, and establish thereby the much required transparency. It is important that minority shareholders are equipped with high quality objective facts and figures from the boards on compensation decisions, rather than basing their decisions, which are important, on subjective opinions or narratives provided by the media. Through my study, I show that the pay performance sensitivity of promoter CEOs is not made as transparent, as it needs to be to establish legitimacy to the decisions made by the boards by minority shareholders. If the compensation design and disclosure models are rightly administered by NRC, in collaboration with institutional investors and proxy advisory firms by disclosing it in easy-to-read language and data tables, it could serve as a transformational tool towards establishing transparency around equitable distribution of a firm's wealth across the shareholder segments. Compensation as a tool, if administered well, can serve as a level playing field between promoter and professional CEOs.

14. Recommendations

Based on my findings, I establish that the present quality of the regulations placed around the disclosure of executive compensation in annual reports of Indian firms does not provide sufficient detail, necessary for a minority shareholder to be able to review and make a decision to cast his/her vote to the proxy proposal, and thereby approve / reject the pay levels of executives. Essentially, this goes against the spirit of the larger corporate governance process aimed at involving a wide range of retail shareholders in the governance process. Significant level of data gathering, and analysis skills are required before a meaningful inference can be made on the linkage between pay and performance. The section in the annual report that describes the variable pay component only provides a high level and non-specific references to factors that are included under the 'performance' definition.

14.1 Improve disclosure quality on pay versus performance

Recent changes done to the Dodd-Frank act by SEC in 2022 are highly progressive in nature in addressing this challenge; and the changes outlined in Section 14(I) added to the Securities Exchange Act of 1934 provide a blueprint of the direction that can be taken by SEBI to improve the quality of disclosures related to executive pay, and resolve issues of transparency that still exist. The proposed rule went into extensive comment period from 2015, and was reopened in January 2022. The final rule, referred to as 'pay vs. performance rule' created a new Regulation S-K item 402(v), which specifies the disclosures that must be made under different types of filings to disclose information about the relationship between executive compensation and financial performance. The new rule requires firms to quantify and describe, in both tabular and narrative format. There must be a clear description of the relationship between compensation actually paid to executives, and the firm's financial performance across multiple metrics.

The tabular format disclosure should cover the last five fiscal years, although for the first year, only the last three fiscal years are required, with an additional year added over the next two years of disclosure.

Following the tabular format is mandatory with a row for each covered year. Compared to the amounts currently provided in the Summary Compensation Table ("SCT") and Compensation Discussion and Analysis ("CD&A"), the table is meant to give investors uniform data on executive compensation in a way that makes it easier to link to corporate performance. As a result, the table contains both the current SCT amounts and the newly determined ‘actually paid’ compensation. The table also requires companies to compute their cumulative total shareholder return (TSR) and TSR of a peer group for each year covered in order to give investors standardized data on company performance. In a similar vein, businesses must incorporate a calculation of their net income, and an additional financial performance measure selected as by the company. Unlike other existing ‘principles-based’ compensation disclosure obligations, the table must be included in the manner specified by the new rule in order to enable comparisons between companies.

14.2 Pay versus Performance Table

Year	Summary Compensation Table Total for PEO	Compensation Actually Paid to PEO	Average Summary Compensation Table Total for Non-PEO Named Executive Officers	Average Compensation Actually Paid to Non-PEO Named Executive Officers	Value of Initial Fixed $100 Investment Based On:		Net Income	[Company-Selected Measure]
					Total Shareholder Return	Peer Group Total Shareholder Return		

Source : SEC Adopts Pay Versus Performance Disclosure Rules | Publications | Kirkland & Ellis LLP (Kirkland & Ellis)

*The detailed definitions covered in this section 14.2 for each of the field in the table above are provided in the SEC Pay versus Performance Final Rule documents. Definitions provided in the **italics** below in this section are the summaries from Kirkland & Ellis (Source : Kirkland & Ellis . SEC Adopts Pay Versus Performance Disclosure Rules: https://www.kirkland.com/publications/kirkland-alert/2022/09/sec-pay-versus-performance-disclosure-rules)*

***Total Compensation Paid:** The total compensation paid to (i) the registrant's principal executive officer ("PEO") and (ii) as an average, the registrant's other named executive officers ("NEOs").*

- *This will be the amount reported in the Summary Compensation Table for the applicable fiscal year.*

***Compensation Actually Paid:** The compensation actually paid to (i) the PEO and (ii) as an average, the other NEOs. This amount will reflect the total* *compensation reported in the Summary Compensation Table, but with the pension values and equity awards adjusted as follows:*

- ***Pension Values:*** *adjusted by, (i) subtracting from the Summary Compensation Table total the aggregate change in the actuarial present value of all defined benefit and actuarial pension plans, and (ii) adding back the aggregate of the following two components:*
    - *The actuarially determined service cost for services rendered by the executive during the applicable fiscal year; plus.*
    - *The entire cost of benefits granted in a plan amendment (or initiation) during the covered fiscal year that are attributed by the benefit formula to services rendered in periods prior to the plan amendment or initiation.*
- ***Equity Awards****: adjusted by (i) subtracting the grant date fair value of the equity award amounts reported in the Summary Compensation Table for each applicable fiscal year, and (ii) adding or subtracting, as applicable, for each applicable fiscal year as follows:*
    - *Adding the year-end fair value of any equity awards granted in the covered fiscal year that are outstanding and unvested as of the end of the covered fiscal year.*
    - *Adding the fair value of the vesting date for awards that are granted and vest in the same covered fiscal year.*

- *Adding the dollar value of any dividends or other earnings paid on stock or option awards in the covered fiscal year prior to the vesting date that are not otherwise reflected in the fair value of such award or included in any component of total compensation for the covered fiscal year.*
- *Adding or subtracting the amount of change as of the end of the covered fiscal year (from the end of the prior fiscal year) in fair value of any awards granted in prior years that remain outstanding and unvested as of the end of the covered fiscal year.*
- *Adding or subtracting the amount equal to the change as of the vesting date (from the end of the prior fiscal year) in fair value for awards granted in prior years that vested in the covered fiscal year; and*
- *Subtracting the amount equal to the fair value at the end of the prior fiscal year for awards granted in prior years that are forfeited during the covered fiscal year.*

Financial Performance Measures

- *TSR: The registrant's total shareholder return ("TSR").*
  - *TSR (and peer group TSR) must be calculated based on a fixed investment of $100 at the measurement point, on the same cumulative basis as is used in Item 201(e) of Regulation S-K.*
  - *Example: For fiscal year 2020, after looking at the closing stock price on December 31, 2019, and on December 31, 2020, it is determined*

that the stock price increased by 25% over such period. The registrant would then multiply $100 by 125% and report $125 in the table for fiscal year 2020.

- *Peer Group TSR: The TSR for the registrant's peer group.*
  - *The peer group used for this tabular disclosure must be either (i) the peer group used by the registrant for purposes of Item 201(e) of Regulation S-K (the "Industry Peer Group") or (ii) the peer group used in the registrant's CD&A for purposes of disclosing compensation benchmarking practices (the "Compensation Peer Group").*
  - *If the registrant changes the peer group used in this tabular disclosure from a peer group that was used in a previous fiscal year, appropriate footnote disclosure must be included.*
- *Net Income: The registrant's net income.*
- *Company-Selected Measure: The registrant's "Company-Selected Measure." This is a financial performance measure selected by the registrant that represents the registrant's most important financial performance measure (that is not otherwise required to be disclosed in the table) used by the registrant to link compensation actually paid to its NEOs to company performance for the most recently completed fiscal year.*

14.3 iXBRL enablement

Inline XBRL tagging of these key data elements of disclosure in the filings immensely help enable data providers, proxy advisors and compensation consultants to collect most authentic and accurate data trends without any manual errors. This technology embracement as a mandatory process enables market professionals in the field of governance to equip retail shareholders with the required data analytics, trend analysis, peer group comparisons with a relevant commentary and insights.

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