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A field guide to shareholder redressal in India

A new class of investors is vocalizing its opinions and casting its vote, rather than exiting their shareholding at the first whiff of a disagreement with management decisions. A look at recent investor engagement and what is driving this change

Indian equity shareholders are increasing their proactive engagement with companies. A new class of investors are vocalizing their opinions and casting their vote, rather than exiting their shareholding at the first whiff of a disagreement with management decisions. A slew of recent instances – United Spirits (where related party resolutions were defeated), Siemens (where shareholders forced the parent to step-up payment for the acquisition), Crompton Greaves (where the deal structure was changed), PTL Enterprises (shareholders got the court to intervene), Tata Motors (shareholders first voted down salary increase, before approving it the second time around), Maruti (over 20 months of negotiations with shareholders, before the company obtained shareholder approval), and many more, discussed in this report, signal this change.

These instances can no longer be seen as one-off instances, but a change in how shareholders are starting to engage with companies. Three developments are responsible for this change:

Change is supported by regulation

The Companies Act, 2013, focuses on governance and a board structure that fosters good behaviour. The Act also requires obtaining approval by majority of minority shareholders for related party transactions. Further the Act has made e-voting mandatory, the real implication of which is in the manner in which the votes are counted. E-voting counts one vote per share held, which dramatically changes the counting from the show-of-hands method (- of counting one vote per hand, prevalent till then). Now each vote counts. Equally important, the implementation of e-voting means that all resolutions, even those which are presented only at shareholder meetings (and not just via postal ballot), have to be polled.

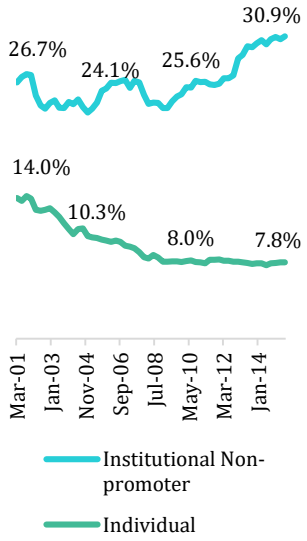
Keeping step with the new act, SEBI too has developed a tighter corporate governance framework. But it was an innocuous circular SEBI issued in March 2010, with corporate governance being just one of the six agenda items, which suggested that the mutual funds play 'a greater role in the better governance of listed companies,' that got mutual funds to focus on voting. It asked funds to have a voting policy and a process to vote their shareholding. With time, SEBI asked for greater disclosure including providing the rational for their pick, forcing investors to be far more thoughtful about their choices.

In fact, on the strength of these regulations, India ranks a surprisingly high 8th, on Protection of Minority Investors in World Bank's 'Doing Business 2016' report.

Indian institutional ownership is now at the 'active engagement' threshold

For long, retail investors were large holders in equity, the promoters held just enough to get themselves re-elected to continue running their business. Domestic institutions, largely government owned, supported the status quo. While 'promoters' have spent the last decade shoring up their shareholding, the retail has given way to FII's and domestic mutual funds, accountable in turn to their depositors. Anecdotal evidence from other geographies suggests that once

% Ownership of Institutions and Individuals in BSE 500 companies



Source: Market data

institutions approach 30% ownership, their engagement with companies deepens. Institutional holdings in India are now at this level (see accompanying chart).

Proxy firms like IiAS have moved bilateral dialogues into a public debate

The voting or proxy advisory firms have catalysed this engagement. This is the third ingredient in the engagement cocktail. IiAS, the oldest, was established in 2010, followed in quick succession by two others. These firms provide commentary and analysis on shareholder resolutions, which are being picked up by the media and disseminated within a larger community.

The various case studies cited have links to the research and commentary that IiAS has provided evidence of the role that advisory firms are now playing. It has resulted in bilateral dialogue giving way to a broader public debate amongst companies, shareholders, media and the regulators.

Shareholders are waking up to the realities of their power – and it's about time they did. If the Indian equity markets are to attract more capital, then shareholders and boards must create an environment of active communication and predictability of behaviour. In the next decade, we hope, the terms of engagement between shareholders and company boards will be less regulatory-driven and more as a good governance practice.

This report updates investors about recent instances where shareholders have engaged with companies on strategy and governance issues.

To prepare this report, IiAS met multiple investors, legal professionals and other stakeholders (banks, regulatory entities), to document some governance events and the actions undertaken, with the intention to provide a rough guide to the kind of actions that can be undertaken within the current corporate governance and regulatory framework.

This report is divided into three parts including annexures:

- **Part I:** The report focuses on investors in listed companies with relevant case studies and options to address corporate malfeasance. These are analysed within a framework for engagement (by stakeholders) postulated by renowned economist Albert O Hirschman.
- **Part II:** This section is focused on the challenges faced by private equity investors, the key learnings and what practical steps investors are taking to address concerns.
- **Annexures:** Indian law contains a number of remedies for minority shareholders who are aggrieved or feel short-changed by majority/promoter action. These are contained in common law as well as statute - the erstwhile Companies Act, 1956 ("1956 Act") and the new Companies Act, 2013 ("Act"). Yet, while working with investors, IiAS finds equity holders- both long only market investors and private equity (PE) funds, unclear about what the remedies are or who can give them relief. The Annexures list out the options available to shareholders to enforce their rights within the regulatory framework.

Investors should note that the data provided on specific companies is based on publicly available information sources. This guide is not meant to be exhaustive and does not constitute legal advice.

Mukul Nag, Advisor: IiAS, has co-authored this publication.

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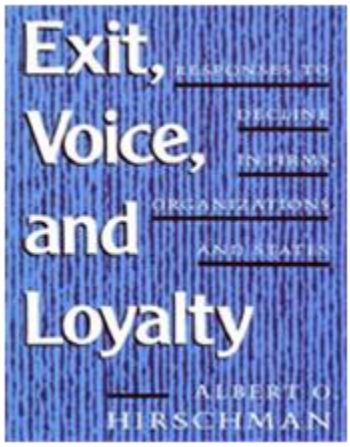
Part I: Investors in Listed Companies

A framework for engagement

Albert O Hirschman's 1970 highly regarded treatise "Exit, Voice and Loyalty" remains as relevant today as when it was written first in 1970. The book provides a framework that can be particularly useful for investors as they think about their engagement with companies.



The essay stated that any form of human groupings (such as the stakeholders of a listed company), have essentially two possible responses when they perceive that the organization is demonstrating a decrease in quality or benefit to the member:

1. Exit: investors vote with their feet, which, at time, may entrench the status quo or even reinforce the cycle of decline; or
2. Voice: investors attempt to improve their relationship by voicing their complaint/ grievance – essentially, engaging with company management.

Exit and Voice themselves represent a union between economic (buy and sell) and political (raising concern on the issue) action.

Hirschman demonstrated that 'Loyalty' (corresponding to a stakeholder's interest in the organizations success) determines the choice between Voice and Exit.

In the equity market, the factors of 'Loyalty' could include the importance of the company in its industry, potential valuation upside in medium term and the impact of liquidity discount on valuation at exit when multiple investors try to sell.

IiAS' experience with recent corporate governance challenges faced by market investors

Institutional and individual investors in listed corporates have played a more proactive role in recent times to address perceived corporate governance transgressions by both domestic and multinational entities. Some recent examples are listed in the box 1 below.

A review of recent instances discussed in the following pages) provide an illustration of how stakeholders can engage with company managements to address their concerns and assert their rights. In several of these cases (Maruti Suzuki India Limited and Akzo Nobel), investors chose to remain invested rather than exit the stock, on account of 'Loyalty'; and, for the most, they have benefitted from their engagement with the companies. Where managements refused to engage or address concerns, shareholders have taken legal recourse (the Kerala State Government in PTL Enterprises and The Children's Fund in Coal India).

In some of the cases discussed, engagement (Voice) has played a key role. Maruti Suzuki, Akzo Nobel, Siemens, are all cases where investors have been in dialogue with the company to sort through issues. While for the most their Voice has been passive but firm, in the case of PTLE, the state government as shareholder chose to raise its Voice by opting for legal recourse.

Investors have to constantly engage with corporates on a variety of issues. This could be corporate action (the proposed merger of Cairn Energy into Vedanta Ltd. at what is seen as adverse swap ratio terms for minority shareholders of Cairn Energy), specific decisions (Dr. Mallya continuing on the United Spirits Limited 'USL' board even after the USL Board has passed a resolution that it had lost confidence in him - this matter is sub-judice) or governance structures (the need for Government to follow corporate governance norms in the appointment of independent directors to public sector undertakings 'PSU's', especially banks).

This is the right time for investors to deliberate on how they plan to take their agenda forward.

Box 1: List of companies in which shareholder resolutions have been defeated

	Company	Meeting date
1	Bharat Electronics Ltd.	3-Sep-15
2	Camson Biotechnologies Ltd.	24-Sep-14
3	Coal India Ltd.	10-Sep-14
4	Dhanlaxmi Bank Ltd.	20-Sep-14
5	Eros International Media Ltd.	28-Dec-14
6	Gayatri Projects Ltd.	28-Sep-15
7	Hindustan Zinc Ltd.	24-Jun-14
8	I F C I Ltd.	27-Aug-14
9	I L & F S Transportation Networks Ltd.	21-Aug-14
10	Mcleod Russel India Ltd.	30-Sep-15
11	Multi Commodity Exchange Of India Ltd.	29-Sep-15
12	Orient Refractories Ltd.	20-Sep-14
13	Panacea Biotec Ltd.	25-Sep-14
14	Repco Home Finance Ltd.	12-Sep-15
15	Siemens Ltd.	17-Sep-14
16	Steel Authority Of India Ltd.	23-Sep-14
17	Tata Motors Ltd.	27-Jun-14
18	United Spirits Ltd.	28-Nov-14

Case studies of engagement by market participants

Maruti Suzuki India Ltd. (Maruti): Deal terms re-worked

Shareholders' concern	• On 28 January 2014 Maruti announced that its 56% parent, Suzuki Motor Corporation, Japan (SMC) would set up a factory in its wholly owned subsidiary in Gujarat to manufacture vehicles. The vehicles would then be sold to Maruti, who in turn will sell these in the Indian market. • Maruti could afford to set up the Gujarat plant on its own, given it held over Rs.90 bn in liquid assets. If it did not invest in the Gujarat plant, what would it do with those funds? • Over a period of time Maruti would not remain a manufacturer and eventually become a 'marketing' company, which would impact its valuation over time. • Maruti had timed the announcement to avoid a shareholder vote – the new regulations were to be notified in April 2014 under which a majority of minority shareholder vote would be required to approve this transaction.
Steps taken by shareholders	• On 13 February 2014 some of the largest institutional investors sent a joint letter to the Board of Maruti questioning the rationale for letting SMC set up the Gujarat plant through a 100% subsidiary. In the letter, investors also sought details on the calculation of the return on investment proposed to be provided to SMC. • This was followed by a second letter on 5 March 2014, seeking feedback on the fiduciary role played by independent directors in evaluating the offer from SMC and whether other offers/ options were considered. • A third letter raised governance concerns. It was also reported that a few independent directors had questioned the original Board decision and had sought greater information on key aspects of the deal. • Post meetings with institutional investors, Maruti was compelled to rework the proposal to plug potential sources of leakages as identified by investors. Moreover, Maruti also agreed to bring the transaction to a vote (although not required by law, at the time it was first proposed).
Result of shareholder engagement and current status	• From January 2014, Maruti waited for over 18 months before bringing the transaction to vote – by which time, SEBI reduced the resolution passing threshold by minority shareholders to >50% from the earlier 75%. • The arrangement was approved by shareholders in December 2015

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- Gujarat Announcement 28 Jan 2014
- Has Suzuki short-changed Maruti? 4 Feb 2014
- Maruti must invest in the Gujarat plant 4 Mar 2014
- Legal recourse for Maruti Shareholders 14 Mar 2014
- Maruti launches the razzmatazz 9 June 2014
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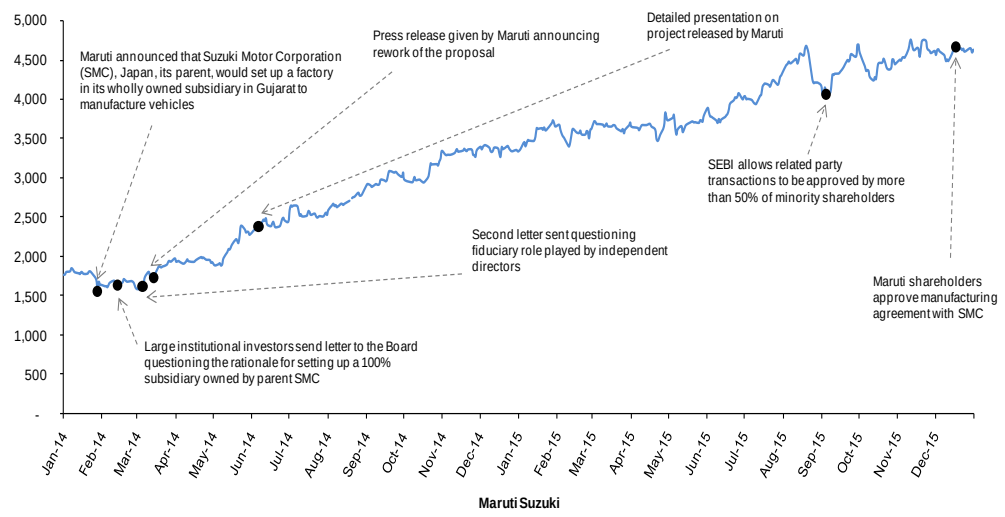
- Open letter to the shareholders of Maruti November 2015



United Spirits Ltd. (USL): Shut the funding tap on non-viable group companies

Shareholders' concern	• There were several undisclosed transactions undertaken by USL with the Dr. Mallya-owned UB group that regulatory changes compelled to be disclosed and put to shareholder vote. These were not business critical transactions and effectively resulted in fund leakages to the UB group. • USL's balance sheet had been used to for onward lending to Kingfisher Airlines (KYA), which was discovered and disclosed only after Diageo took over operational management. • Dr. Mallya continued as USL's Chairperson at a time when he was personally mired in a controversy of being labelled a wilful defaulter with respect to KYA loans. If it was legally established that Dr. Mallya was indeed a wilful defaulter, it would impact USL's ability to access the Indian banking sector. • Investors were concerned about related party transactions and the opacity around resolutions that were being brought to them for approval around the time the company was unable to present its accounts.
Steps taken by shareholders	• On 28 November 2014, nine out of 12 resolutions presented in a postal ballot were voted against by the minority shareholders. ○ The nine resolutions that were rejected included related-party transactions under which the cash-strapped UB Group (owned by Dr. Mallya) stood to earn an estimated over Rs 8.0bn in revenue over the next few years from United Spirits plus a Rs 13.37bn loan. • Irate shareholders also voted against the licensing transaction between USL and Diageo. • Separately, another UB group company, Mangalore Chemicals and Fertilizers Limited, coerced Dr. Mallya's resignation from the board
Result of shareholder engagement and current status	• The Diageo brand licensing proposal related resolution was subsequently resubmitted to shareholders with a lot more disclosure and a strong business case for the transaction. Shareholders approved the resolution. • Despite shareholder opposition, Dr. Mallya was re-appointed as Chairman of USL as Diageo was bound under a shareholder agreement to support his candidature. • Post the forensic audit, the USL Board noted that they had lost confidence in Dr. Mallya continuing in his role as Chairman and called upon him to resign as a director/ Chairman of the Board. Dr. Mallya is fighting this decision and claims that, under the shareholder agreement, he has a right to the board seat.

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- IiAS Voting Advisory AGM 30 Sept 2014
- Mallya's appointment and Diageo's silence 7 Oct 2014
- IiAS Voting Advisory United Spirits EGM 28 Nov 2014
- Mallya must step down, but is Diageo really the victim? 27 April 2015
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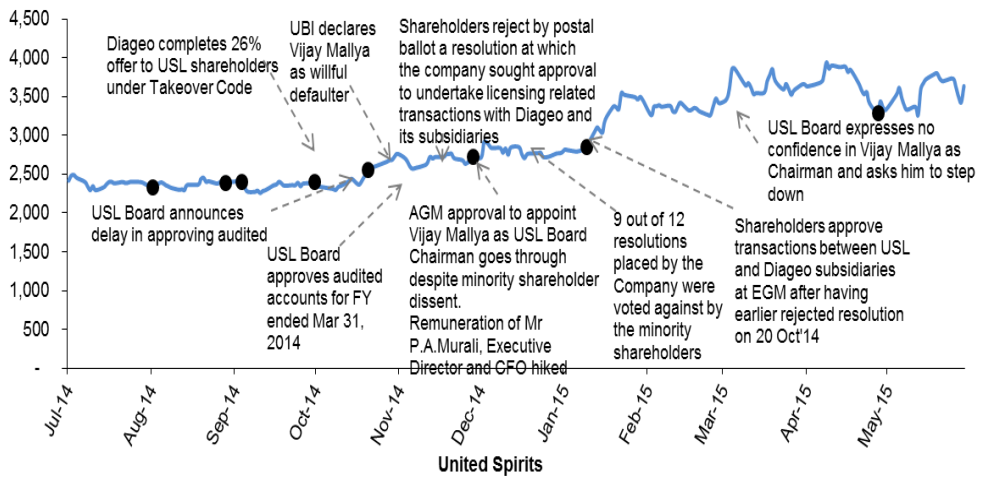
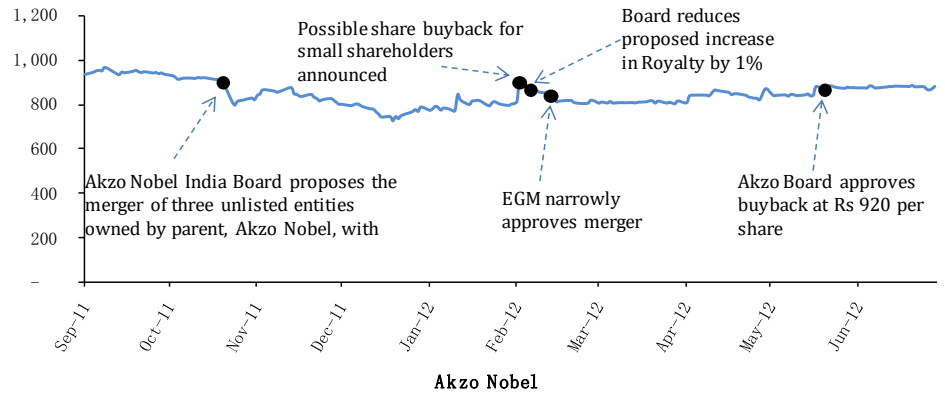


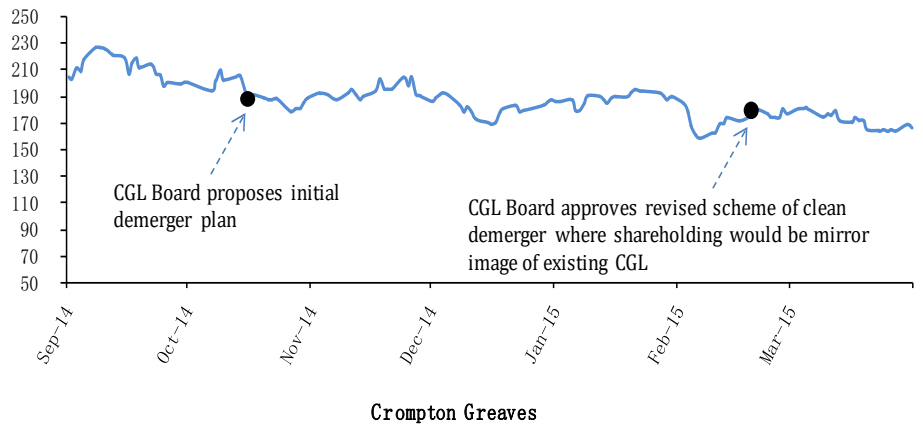
Akzo Nobel India: A give-and-take between investors and the company

Shareholders' concern	• On 21 October 2011, the board of Akzo Nobel India (listed) proposed the merger of three unlisted entities owned by parent, Akzo Nobel, with itself on terms that were perceived to be biased against minority investors. • In addition, royalty payment to the MNC parent was proposed to be increased from 1% to 3%.
Steps taken by shareholders	• IiAS organized a joint meeting of institutional investors who then interacted with Akzo's local management. IiAS held proxies on behalf of individual shareholders and voted against the proposals. • Institutional shareholders voted against the resolutions; but two institutions abstained (contrary to their earlier position), due to which the resolution was passed by a narrow margin with 76.33% votes in favour.
Result of shareholder engagement and current status	• The Company agreed to partially roll back the proposed royalty increase (reduced from 3% to 2% - though it would subsequently move up). • The company also offered a buyback to provide shareholders with an option to exit.



Crompton Greaves Ltd. (CGL): When market pressure actually worked

Shareholders' concern	• On 16 October 2014, the CGL Board approved the demerger of the consumer businesses. It was proposed that Crompton Greaves Consumer Electrical Ltd. (CGCEL), the consumer business, would continue to be held by CGL through a 25%+ 1 share stake while the balance stake would be a mirror of the shareholding pattern of the existing CGL. Post demerger, the CGL promoters would continue to control ~43% of CGL and critically increase it to 57% (32%+25%) over the more attractive CGCEL business. • The demerger would unlock shareholder value, yet the continued 25% holding of CGL was seen to be a veiled attempt to increase control over CGCEL by promoters.
Steps taken by shareholders	• IiAS criticised the demerger terms and the press reported that it would recommend that minority shareholders vote against the proposal. • Brokerage houses panned the demerger structure as unfavourable to minority shareholders as CGL's 25 per cent stake in CGCEL would not fully unlock value for minority shareholders. • The stock exchanges asked the company to seek shareholder approval prior to proceeding on the demerger scheme.
Result of shareholder engagement and current status	• CGL was quick to understand that the proposal may be rejected by shareholders. Therefore, in February 2015, CGL's Board approved a revised scheme of demerger, under which CGCEL's shareholding would completely mirror that of CGL's – promoters would not control an incremental 25% in CGCEL. • Subsequently, PE investors Advent and Temasek agreed to acquire the promoters' stake in CGCEL.



PTL Enterprises Ltd. (PTLE): Sale of material business stopped – for now

Shareholders' concern	• At the AGM on 22 September 2014 PTLE proposed the sale of its entire shareholding in two hospitals (Artemis Health Sciences/ Artemis Medical Services) to promoter-owned Leto Healthcare Private Ltd., at very low (and inexplicable) valuations. • The proposal was sought to be approved just prior to more stringent SEBI listing agreement norms that required only minority investors to vote on related party transactions (RPT) coming into effect from 1 October 2014.
Steps taken by shareholders	• A few large retail shareholders worked with IiAS to bring out the concerns on the deal which led to questions being raised in the Kerala State legislature. • Shareholders also wrote to the promoter, Onkar Singh Kanwar, the company's independent directors and the Government nominee director, seeking that the resolution not be tabled – but, under e-voting rules, the resolution could not be withdrawn once the voting process had begun. Therefore, the company stated that it will continue to present the resolution at the AGM. • KSIDC, a Government of Kerala owned entity and a 2.27% shareholder, got a stay against the proposal to sell the healthcare businesses by PTLE and sought an investigation into the affairs of the company.
Result of shareholder engagement and current status	• The company did not take up the resolution at the 22 September 2014 shareholder meeting due to the stay granted by the Kerala High Court. • The company seems to have put the Artemis sale plans on hold, as it has not brought back the proposal to shareholders till date. • In case the proposal is brought to shareholders to vote, the more stringent SEBI norms with regard to shareholders' approval for RPT's i.e. approval of majority of minority investors will apply.

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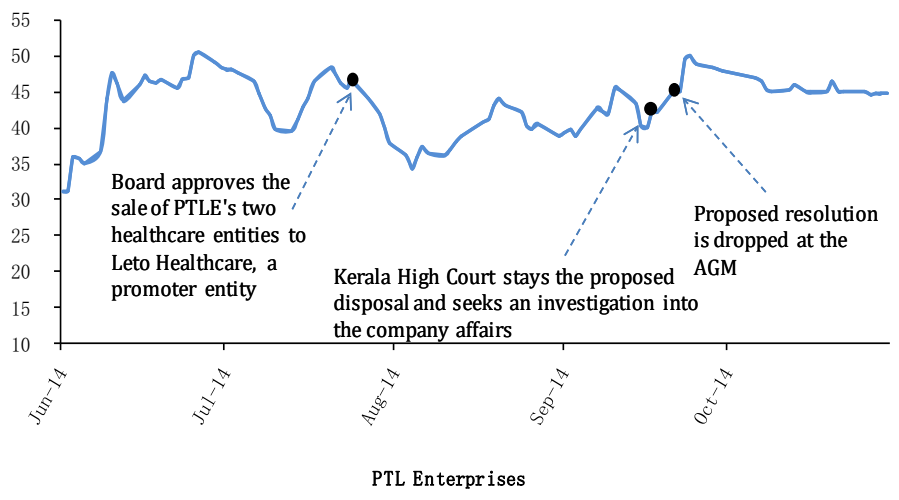
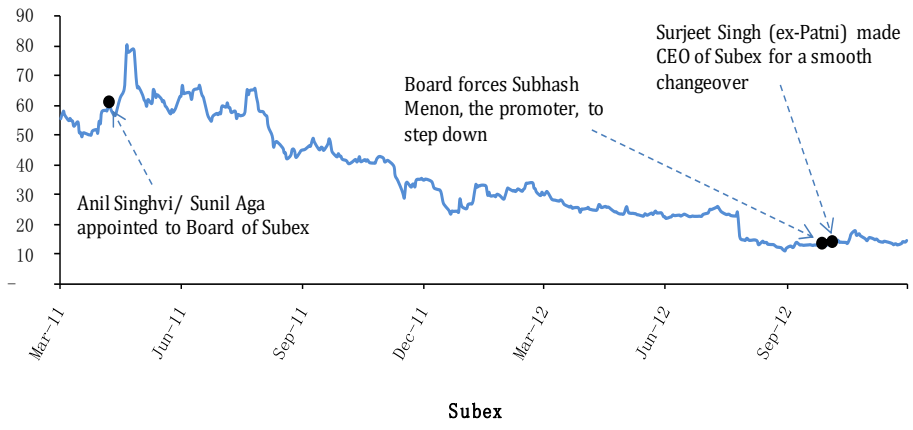


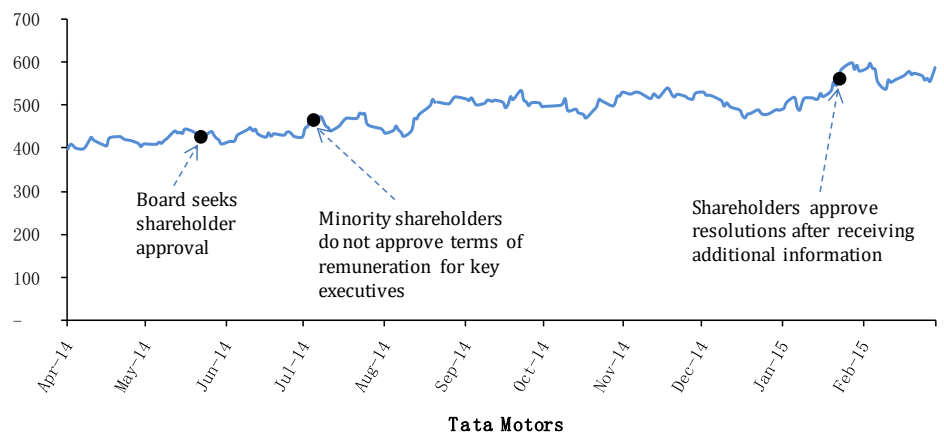
Subex Ltd.: Change in management

Shareholders' concern	• Syndesis, acquired by Subex for an all cash deal in 2007, saw its business nosedive from 2008 and put immense pressure on the business/ financials of Subex. • The company was unable to repay the large USD 180mn foreign currency convertible bonds (FCCB) raised in 2007 and had to first restructure the FCCB in 2009 and then again in 2012.
Steps taken by shareholders/ board	• The FCCBs were acquired at a discount by two funds, Elliot and QVT, which converted a part of the FCCBs into an equity stake of ~20%. • The company appointed Anil Singhvi (*Note: he is one of the founders of IiAS*) and Sanjeev Agha, in 2011 as independent directors. • The Subex board felt the company had been unable to channel the software and telecom talent within Subex to come up with new product lines since the 2007 Syndesis debacle. • Subhash Menon, the promoter, saw his shareholding fall to just over 5%. This was expected to fall further to just 2% on further conversion of outstanding FCCBs. • The Board decided to seek a change in the management of the company as the business underperformed and promoter's stake became negligible.
Result of shareholder engagement and current status	• Supported by Elliot and QVT, the Board pressed Subhash Menon to step down in September 2012. • Surjeet Singh (ex-Patni) was made CEO of Subex for a smooth changeover in the management.



Tata Motors Limited: Additional disclosures convince shareholders

Shareholders' concern	• In May 2014, Tata Motors Limited[1] (Tata Motors) approached shareholders for an approval of the remuneration of three executive directors, one of whom was the late Karl Slym (MD). Since Tata Motors had reported standalone losses during that year, it needed shareholder approval to pay remuneration at those levels.
Steps taken by shareholders	• Shareholders voted against these resolutions citing that there was not sufficient rationale for payouts of the remuneration, especially given that Tata Motors was reporting losses at the standalone level.
Result of shareholder engagement and current status	• The company began engaging with shareholders explaining the rationale for the remuneration. Following this, the company re-presented the same resolution, albeit with far greater disclosures and explanations, in January 2015. • Shareholders passed the resolutions when they were presented for approval the second time.



[1]*Tata Motors and Tata Investment Corporation Limited (TICL) are a part of the Tata Group. TICL is a shareholder of IiAS.*

Siemens India Ltd. (Siemens India): More granular disclosures and a higher transaction value

Shareholders' concern	• On 7/ 8 August 2014 the Board of Siemens India proposed to sell its metals technology (MT) business at a valuation of ~Rs 8530 mn to its German parent, Siemens AG. After the purchase by Siemens AG, the MT business was to be transferred to a joint venture between Siemens AG, Mitsubishi Hitachi Metals Machinery and Mitsubishi Heavy Industries. • The valuation was lower than the value at which Siemens AG had transferred/sold the business to Siemens India, three years earlier, as a part of a scheme of amalgamation of Siemens VAI Metal Technologies Pvt Ltd. and its wholly owned subsidiary, into the listed Siemens India.
Steps taken by shareholders	• The transaction was a related-party transaction, which required the resolution to be passed by 75% of minority shareholders present and voting. Minority shareholders rejected the resolution as the valuation of ~Rs 8530 mn was seen as being low and below the acquisition price at which it was completed three years earlier.
Result of shareholder engagement and current status	• A committee of the Siemens India Board was constituted that considered and approved a revised offer from Siemens AG of Rs 10230 mn (a ~20% increase; the valuation of the earlier merger). • In Nov 2014, a revised resolution with far greater disclosures, including the financials of the MT business, reasons for poor performance of the business and an additional Fairness Opinion by ICICI Securities (on the Grant Thornton valuation) was placed before the minority shareholders. The shareholders approved this resolution.

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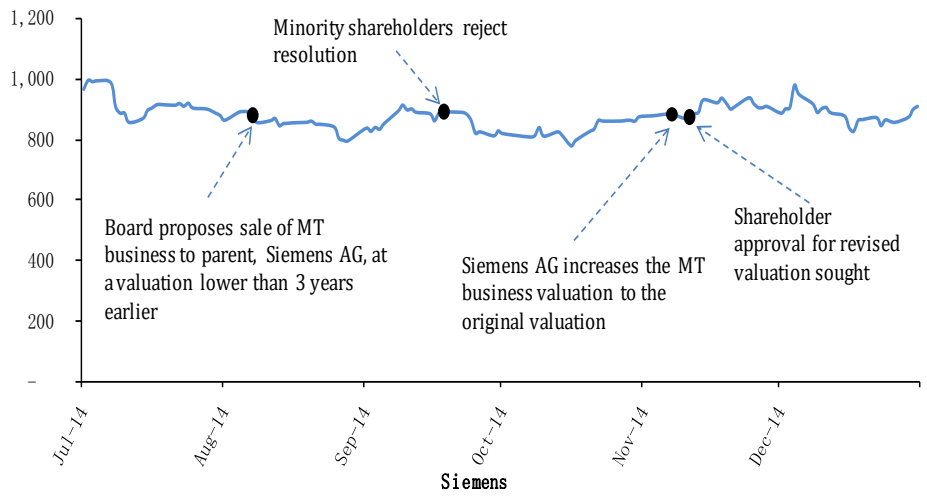
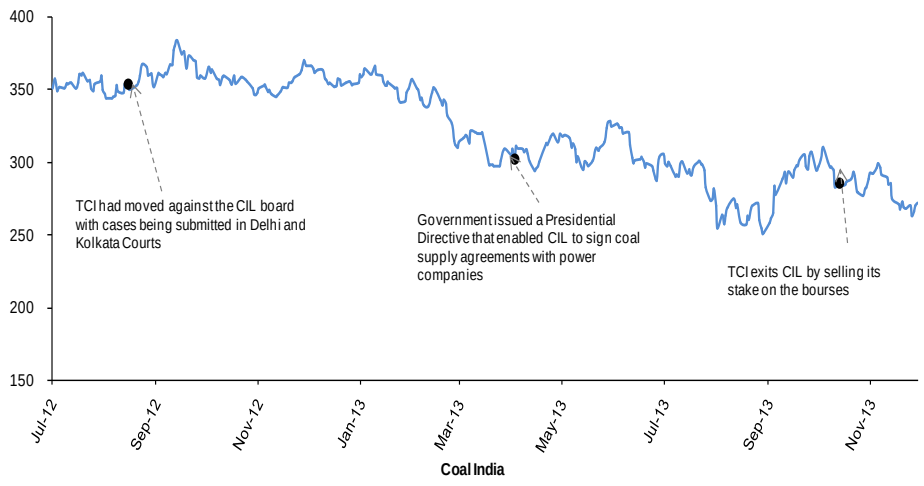


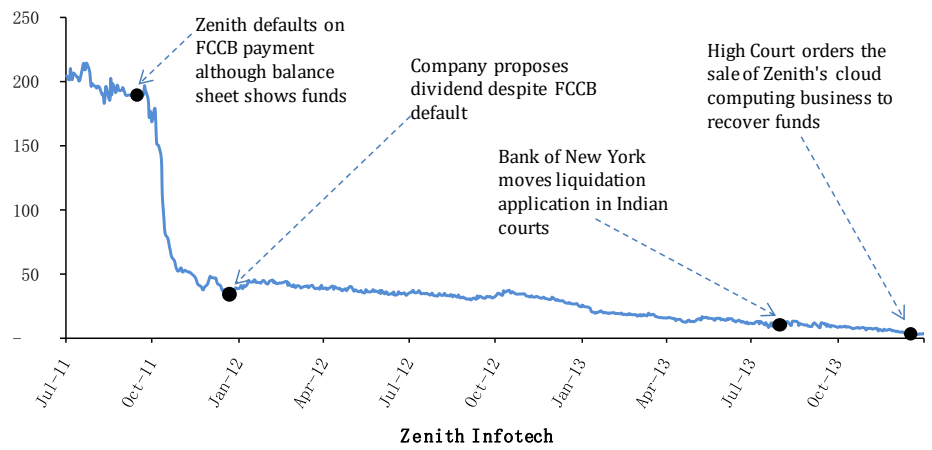
Coal India Ltd. (CIL): Struggle against the power of the Government

Shareholders' concern	• The Children's Investment (TCI) Fund Management LLP, a prominent activist fund, accused the CIL management of not protecting minority shareholders' interest and harming the company by signing fuel supply pacts for coal with power producers at prices lower than the market rate. It also alleged delay in the installation of washeries, inefficiency in underground mining and other actions which adversely impacted value of the business.
Steps taken by shareholders	• TCI had moved against the CIL board in August 2012 with cases being submitted in Delhi and Kolkata Courts. • TCI cited selling coal to power companies at below 70% of cost, and accused the Indian Government of mismanagement and political interference against the interest of minority shareholders. • After filing the suit, TCI had converted it into a representative action suit, which allowed other shareholders of Coal India, with similar grievances to join the petition. • Customers of CIL who benefited from lower coal prices (such as Damodar Valley Corporation) joined CIL in defence of the suit.
Result of shareholder engagement and current status	• Government took a position that in its offer document, CIL had clearly stated the risks associated with government intervention and policy decisions that favour national interest. • The Government issued a Presidential Directive – a rarely used power under Article 53 of the constitution that enabled the company to sign coal supply agreements with power companies. • TCI struggled to effect changes in CIL's governance structure and it exited its ~2% stake (the largest minority shareholder) in late 2013 and withdrew its cases.



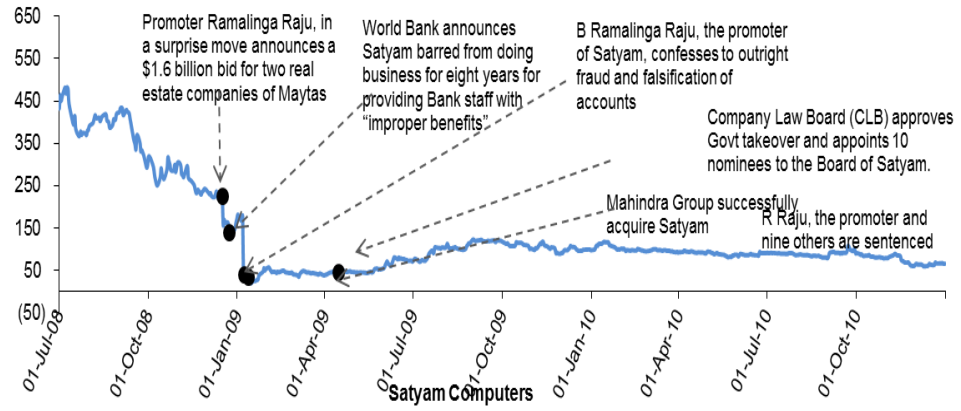
Zenith Infotech Ltd.: Investors get support from the courts

Shareholders' concern	• Zenith Infotech defaulted on payments due in September 2011 to its FCCB's bondholders, although its balance sheet showed it had funds in its bank account. • The Company even proposed a dividend to its shareholders after defaulting to the FCCB bond holders.
Steps taken by shareholders	• On behalf of the FCCB holders BNY-Mellon moved a liquidation application in the Indian Courts. • In December 2013 the High Court ordered the sale of Zenith Infotech's cloud computing business to recover funds and pay bond holders; it also noted potential diversion of funds from the earlier sale of another division.
Result of shareholder engagement and current status	• The company has appealed to the Supreme Court against the order for liquidation. • However, there is still no clarity on the illegal diversion of funds to entities overseas and related parties after its earlier sale of another division (Managed Services) in September 2011.



Satyam Computer Services Ltd.: What the Government can do – if it decides to act

Shareholders' concern	• On 7 January 2009, B Ramalinga Raju, the promoter of Satyam, then a Top 5 Indian IT services company, confessed to fraud and falsification of accounts. • As a leading Indian IT services firm, the fraud could have a significant negative impact on the trust factor for the global IT business of Indian companies.
Steps taken by shareholders/ government	• The Government moved swiftly to take over the management of the company post approval from the Company Law Board (CLB) and appointed 10 nominees to the Board of Satyam. • Continuity of the Satyam business for clients and its employees were given priority. • The Government appointed a committee of eminent persons to run a transparent sale process within 6 months of the scandal breaking out.
Result of shareholder engagement and current status	• The well regarded Mahindra Group successfully acquired the asset and combined it with their existing IT business. • R Raju, the promoter and nine others were sentenced to imprisonment and fines in April 2015 after a judicial process lasting over seven years.



What choices can you exercise as a market investor: A quick guide

Actions	Regulatory Perspective	Comments
Send questions in advance to the company management	Shareholders can raise questions/ seek additional information on specific resolutions before taking a considered decision on their response to a resolution.	This has been used effectively to: • get additional information on specific resolutions. IiAS writes to companies as a shareholder and seeks additional information that forms part of its voting recommendations (e.g. from Tata Motors on employee compensation). • convey investor concern through the nature of the queries raised (e.g. queries raised by institutional investors on plans of Maruti); and • use the additional data to create a common platform amongst investors (e.g. in Akzo Nobel India case to get merger valuation details and again in Maruti)
Shareholders can requisition the Board to call an extraordinary general meeting (EGM).	Section 100 of the Act directs the Board to call an EGM on a requisition made by the shareholders of the company who hold, as on the date of the receipt of such requisition, not less than 10% the paid-up share capital of the company. If the Board does not respond within a specified timeframe, the EGM can be called and held by the requisitionists themselves within a period of 3 months from the date of the requisition.	Disgruntled shareholders of S Kumars Nationwide requisitioned the company EGM to discuss alleged mismanagement by the existing management. That this was turned into a farce was an unfortunate conclusion to the meeting (*See IiAS note S Kumars: The Unofficial Minutes*).
Vote against the resolution at the general body meeting.	Section 188 of the Act read with Rule 15 of the Companies (Meetings of Board and its Powers) Rules, 2014 mandates that a company must obtain the prior approval of the majority of the minority shareholders for the purpose of entering into any stipulated related party transaction (RPT).	The requirement that all RPTs need majority of minority shareholders' approval has strengthened and been the major driver of shareholder activism in India in recent years. In unlisted companies however, only interested parties will not vote but other related parties can vote **(very relevant for private equity investors)**.

Actions	Regulatory Perspective	Comments
Approach SEBI seeking action against the company and management. (***Contact details:*** Securities and Exchange Board of India (SEBI), Plot No. C 4-A, G Block, Bandra Kurla Complex, Bandra East, Mumbai-400051 Tel : +91 22 26449950/ 40459950 *Mail ID:* http://scores.gov.in) SCORES is a web based centralized grievance redress system of SEBI*(refer Annexure 5)*	Shareholders can file a complaint to SEBI to take actions under Section 11A and Section 11B of the SEBI Act, 1992 for the protection of shareholders interest.	Maruti institutional shareholders threatened to use this route to put pressure on the Maruti Board to reconsider its decision to set up a new plant wholly owned by its parent.
To file a complaint of oppression and mismanagement under Sections 241and 242 of the Act before the National Company Law Tribunal (currently applicable to CLB under sections 397/ 398 of the applicable Companies Act 1956). To make an application to the Tribunal for an investigation into the affairs of a company. (***Contact details:*** Company Law Board (CLB) Paryavaran Bhawan, B-Block, 3rd Floor, C.G.O. Complex, Lodhi Road, New Delhi – 110 003 Tel: +91 11 24363451 (Secretary, CLB) Fax: 011 – 24361235 (CLB Secretariat) *Mail ID:* secy.clb@nic.in) *(refer Annexure 6)*	Section 244 of the Act provides that a set of shareholders of a company have the right to apply under Section 241 of the Act, to the Tribunal for relief in a case of mismanagement or oppression. This application can be made in case of a company having a share capital, by not less than one hundred members of the company or not less than one-tenth of the total number of its members, whichever is less, or any member or members holding not less than one-tenth of the issued share capital of the company. In the case of a company not having share capital, not less than one-fifth of the total number of its members.	The private equity shareholders of Reliance Infratel approached the Company Law Board (CLB) under the relevant section of the older 1956 Act to seek redressal. ***Since section 244 of Companies act 2013 is not yet notified, similar provisions under 1956 Act are currently in force.***
Enabling Shareholders Associations/ Action suits against the company and seek reimbursement of expenses out	Section 245 of the Act provides that the prescribed number of shareholders or depositors who feel that the affairs of the	Class action suits are a new form of action introduced by the Act. ***The provisions relating to class action have not yet been notified***.

Actions	Regulatory Perspective	Comments
of Investor Education and Protection Fund.	company are being conducted in a manner prejudicial to the interests of the company or its shareholders or depositors, may file an application before the Tribunal on behalf of the shareholders or depositors to restrain the company from certain actions.	Once it comes into force, this provision could act as a significant deterrent to majoritarian corporate action. While a significant threat, the time consuming legal process in India remains a limitation on the effectiveness of class action suits.
To file a derivative action before the relevant Civil Court against the board of directors of the company as well as the company itself. To approach the relevant Civil Court for a direction to the Central Government to conduct an investigation into the affairs of a company.	The Civil Procedure Code, 1908 provides that in case of any fraudulent, unlawful or wrongful act or omission by the company or its directors, which is prejudicial to the interests of the company or its members or which is oppressive to any shareholders, one shareholder can file a suit for relief on behalf of the other shareholders. Any person on whose behalf, or for whose benefit, a suit is instituted, or defended can apply to the Court to be made a party to such suit.	The Children's Investment Fund (TCI) essentially took this approach in bringing a suit against the Coal India (CIL) Board and the Government of India as its principal investor. While filing the suit TCI allowed other shareholders to join its suit. TCI was unfortunately not successful in affecting change in governance norms at CIL

Additional options that are available to an Investor

Companies that raise funds through a Prospectus

Section 27 of the Act states that a special resolution is required to vary the terms of a contract referred to in the prospectus or objects for which the prospectus was issued. The Act also requires that dissenting shareholders shall be given an exit by promoters or controlling shareholders. The exit price will have to conform to the terms and conditions prescribed under the SEBI regulations.

This clause could be a strong deterrent in the hands of public investors when entities that have raised equity funds attempt to change the objective(s) for which the funds were originally raised. It could also strengthen the hands of a PE investor if it dissents on a proposal to vary a contract or prospectus, in which case it can exit the company at a price ascertained in accordance with the SEBI exit norms.

Where the investor is present on the Audit Committee constituted by the Board

Section 177 of the Act empowers the Audit Committee (constituted by the board of directors) to investigate into any matter pertaining to its powers and responsibilities (prescribed under the said Section 177) or referred to it by the board of directors. The Audit Committee can obtain professional advice from external sources and have full access to information contained in the records of the company.

A member of the Audit Committee (and this is particularly true for a PE investor) can seek a separate forensic audit to review and monitor the auditor's independence and performance, effectiveness of the audit process and monitor the end use of funds raised through public offers and related matters.

What role does media play on issues of corporate governance?

The Indian media has played a constructive role on highlighting corporate governance transgressions by often taking a supportive position and disseminating concerns of shareholders. The media throws light on issues that transgress the spirit (though not the letter) and act as a major pressure point for the regulatory bodies to act on such matters. It also provides a forum for various stakeholders with differing perspectives/ interests to put forward their view. Unfortunately, in an increasingly fractured media environment sustained follow up suffers and interest in any issue tends to flag if not augmented by new developments. As a market investor it is worth keeping the following in view about the role media can play in such situations:

- Institutional investors should develop their media strategy early keeping in view the likely support from other shareholders and in the context of the potential impact on their funds brand and business.
- Simplicity in communicating areas of concern is critical and clearly showcasing the short and long term implications is useful.
- It is worth highlighting the impact of corporate action on small shareholders (a sensitive issue for regulators).
- Finally, the involvement of media is a double edged sword as the position taken by a shareholder on corporate governance would be covered by media in the context of any conflicts of interest of the investor.

Box 2: Practical aspects to consider while seeking redressal	
1	Prior to seeking any redressal of corporate governance concerns, be clear about what you want to achieve. A well-defined strategy should be adopted from the outset. Consider the implications of any actions being made public for the company, its Board and you as a shareholder.
2	Identify who your fellow shareholders are and carry out a detailed analysis of the shareholder list. Identify the shareholders whose views/ objectives are likely to be aligned with yours (e.g. an investor sitting on large corporate gains over a long period of time may prefer to lock-in the gains and exit rather than raise issues with the company).
3	Remain in regular communication with fellow shareholders in order to monitor the level of support for the concern areas.
4	If a proxy fight is expected, ensure proxy forms are submitted on time in accordance with the prescribed timelines including any paperwork appointing corporate representatives
5	If your fund is planning to build a greater stake in a company (or exit), consider and take advice on the implications of insider dealing regulations especially, where discussions with the board may have taken place.
6	Avoid seeking resolutions (requisitioning resolutions u/s 100 of the Act) that may limit the business performance of the company or are frivolous. Any resolutions to be requisitioned should be effective and ultimately bind the company in accordance with its articles in the event that they are passed.
7	Ensure that you have a public relations strategy in place early in the process. The media plays an important role in shaping the public and regulator perception and the pace of response to address the concerns. Concurrently, one must be aware of the potential impact of taking a confrontational approach on the funds brand and business.
8	Any litigation should be the last resort as a) they are very time consuming particularly in the Indian context and unlikely to have an immediate effect b) it sometimes leads to intransigence and parties are unable to reach a mutually fruitful solution.

ENGAGE! ENGAGE! ENGAGE!
Engaging with the company about investor concerns (before putting it in the public domain) is often the best initial step. Understanding the company's perspective, getting additional data and exploring reasonable solutions is better than taking a strong public stance that may not allow flexibility to address concerns in the future.

Part II: Private Equity Investors

What has been Private Equity Investors experience in India?

PE firms have invested ~US$ 60billion between 2003 and 2011 – these investments are ripe for exit. The Jan- early Dec 2015 period has been very encouraging with private equity investors estimated to have returned over $5bn to their investors through a flurry of exits. However, it is estimated that ~50% of the investment during the 2003-2011 period may still not have seen an exit.

The key concerns on the Indian private equity market expressed by limited partners (or LPs who fund PE investors) are relatively poor returns and the inability of the Indian legal system to ensure a just award in case of breach of shareholder agreements/ frauds.

The key points that emerge from our discussions with PE Investors on corporate governance are as follows:

- Differences on the business plans, corporate governance issues especially w.r.t. related party transactions (RPT), adherence to affirmative rights and meeting exit related conditions (e.g. exit mechanism/ terms for exit) are key areas of differences between PE Investors and their investee companies. Reported frauds by investee companies also saw a significant rise as the challenging business environment led to a few promoters taking shortcuts.
- PE investments made during the 2006-2011 period have often faced underperformance against the initial business plan, significant dilution of rights under the shareholder agreements (SHA) and poor ability to exit. This has led to significant differences between PE investors and their investee companies on exit at reasonable valuations.
- There is no substitute to investing behind a good promoter. A positive relationship with the promoter/ investee company is the starting point to ensure compliance with the SHA and ensuring an exit.
- At the time of exit there can be a disconnect between what is seen as the requirements of the promoters and the exit requirements of the PE Investor. PE Investors often need an opportunity/ requirement of promoter to push for an exit by the Investor, especially in unlisted entities. Where multiple investors are involved, the complexity of response by investors increases dramatically.
- There is a broad view amongst PE Investors that in practical terms, legal agreements are still difficult to enforce in India. It is tough to get a fair award in a reasonable timeframe through arbitration/ litigation and these mechanisms end up as a negotiating tool rather than to get a just award. The impact of proposed legislations such as the Commercial Divisions Act and Amendment to Arbitration and Conciliation Bill, 2015 (pending in Parliament) still need to be understood.

Examples of corporate governance challenges faced by PE Investors

Type of Issue	Case Studies
Related Party Transactions (RPTs) that transfer value from the minority shareholders (including PE Investor) to the Promoter	**Case 1: Large telecom infrastructure player being merged with promoter entities at high valuations** Concerns raised on merger of promoter entities at high valuations leading to investor stake dilution. Case filed with CLB seeking quashing of the proposed merger. **Case 2: Undertaking real estate transactions that transfer value to the Promoters** Promoter sought to acquire real estate in the investee company from his wholly owned entity at high valuation. PE Investor finally agreed to higher dividend payment by the investee company as a mechanism to provide greater liquidity to the promoter instead of allowing an unfair real estate transaction.
Abiding by terms of exit agreed	**Case 3: Unwillingness to support the exit required by PE Investor** Post investment, the promoter of a well performing company offered to buy shares at the low 'put IRR'(i.e. a right to sell) assured under the SHA, instead of providing a fair valuation exit (expected exit multiple exceeding 5x). Finally, the PE Investor agreed to share upside beyond a certain IRR to get the promoter to agree to a fair valuation exit mechanism. **Case 4: Drag Along rights not adhered to and revision of terms required for sharing sale proceeds** The promoter had agreed on drag along/liquidity preference for the PE Investor. Unfortunately, the company strongly underperformed but the promoter refused to support the exit process. The promoter finally agreed to exit along with PE Investor when he was assured of certain assured payment which led to lower exit payout to PE Investor. There have been other situations where the promoters have been unwilling to abide by performance linked convertible debt terms that were agreed under the SHA and to converting at assured minimum IRRs agreed under the SHA (which in any case is in the legal grey zone in India).
Leakages of revenues/ profits or outright fraud	Unrealistic business performance commitments in a tough business environment between 2008 and 2014, high valuation expectations along with investment structures (e.g. performance linked entry valuation) that incentivised promoters to "game the system" led to an increase in situations of fraud. This was exacerbated by promoters that retained the old thought process of generating unaccounted cash flow outside the company and PE funds that entered into agreements without adequate diligence and diluted tough conditions that ensure probity in companies. As an example private equity invested in Lilliput Kidswear where the promoter inflated revenues leading to withdrawal of the proposed IPO. Further pressure was brought on the PE investors through a court order

Type of Issue	Case Studies
	gagging any news flow and through demonstrations at the offices of their lawyers. Finally the two PE investors resold their stake to the promoter and exited the business. Fraud has also been reported in companies such as Hanjer Biotech/ KS Oils/ Karuteri Global/ AvitelStudioz/ Resurgere/ Fourcee Infra etc. The unfortunate reality is that PE investors have not been able to extract any significant value from these investments using arbitration or court processes.

How have PE Investors coped with issues of Governance/ Exit?

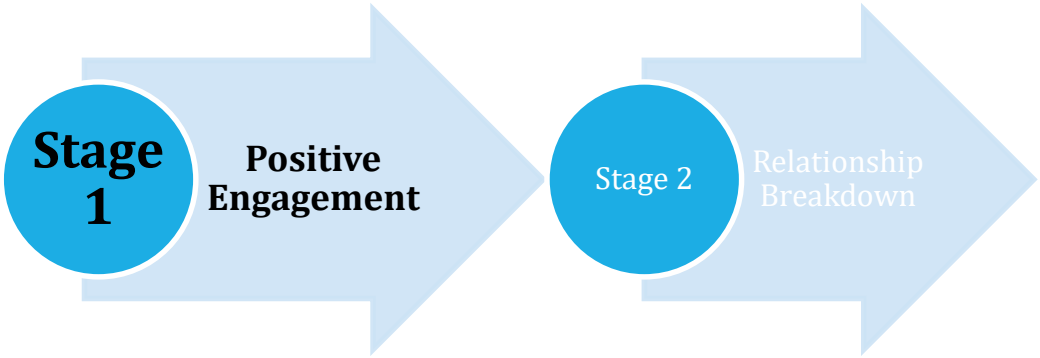
Investors have typically resolved governance and exit issues on a bilateral basis. Usually private equity investors take a "carrot and stick" approach to address difference of opinions on governance aspects.

Confidentiality agreements, sensitivity to limited partner (LP) concerns and potential negative publicity impacting ability to make further investments/ raise funds from investors results in a bilateral closed-door approach being preferred.

This implies that often the legal counsel is the only stakeholder who is privy to multiple such cases.

How do PE Investors engage with investee companies in situations of conflict?

The engagement between the PE Investor and the Promoter can be broadly divided into two stages:



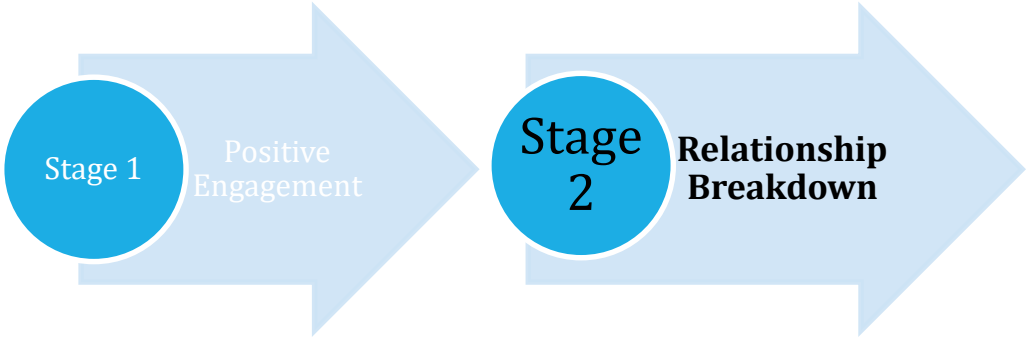
Stage 1: Positive Engagement

At this stage PE Investors typically hold multiple meetings with promoters/ investee companies to get the parties agreed on a mutually acceptable approach on the matter of dispute.

- Usually a specific requirement of the promoter/ company provides the investor an opportunity to create agreement on matters of governance/ exit conditions:
  - Business plan changes
  - Related party requirements
  - Entry into new business segments
  - Difference in approach on capex plans
- Indirect pressure is seen even at this stage as being better than an uncooperative approach.
  - Start raising questions relating to business matters at the Board level that potentially embarrass the promoter in front of his Board members who are often relatives/ friends.
  - Investor takes a tougher stance or actively dissents.
- Using the services of a Forensic Firm could be useful at this stage. Areas that they check that potentially provide influence to the Investor include:
  - Any obvious issues like potential fund leakages.

- Conversations with past employees for any incorrect practices especially which were not disclosed at the time of entering the Investment Agreement (there is often a limited indemnity period that could be relevant in some cases).
- Review of unknown civil/ criminal cases.
- Personal activities that could place the promoter in an awkward position.

- Investor Director seeks areas of dissension to be noted in the board minutes.
  - This is particularly critical under the new Act as liabilities of investor directors have been significantly enhanced.



Stage 2: Relationship Breakdown

At this stage the relationship between the PE Investor and the Promoter/ management has usually reached a point where the terms of SHA are not being followed and significant differences remain post multiple meetings.

- PE Investors at this stage use the rights under 'reserved' matters to:
  - Reject/ seek changes to the business plan.
  - Not accept the borrowing plan (using D: E limits or the business plan route) or its terms.
  - Seek changes to the capex plan or seek further reviews without accepting/ rejecting.
  - Not approve or delay matters relating to related persons.
  - Not accept any board nomination.
- Even in a listed company PE Investors need support of the company/ promoter to exit large 5-20% stakes especially in illiquid Indian companies.
  - A willingness to dump stock in the market could represent a risk to the long term company stock price.
  - However, if the fall in stock price is irrelevant for the promoter or the threat cannot be undertaken by the investor then it becomes a hollow threat.

Why arbitration often does not work...

Shareholder Agreements in India typically provide for arbitration under the Indian Arbitration Act due to investee company insistence and prohibitive costs for overseas arbitration. However, arbitration proceedings in India have often been ineffective as it usually takes 3-5 years to conclude which vitiates the purpose of arbitration.

The reason for significant delay in the arbitration process is as follows:

- Delaying tactics during arbitration (e.g. legal position taken against applicability of arbitration/ lack of agreement on arbitrators to be appointed) essentially brings the arbitration process within the domain of the slow moving Indian court system
- Unfortunately, Indian Courts have also shown a willingness to get involved in arbitration procedures (instead of consciously pushing it back to the arbitration mechanism) leading to considerable delays
- Indian arbitrators tend to take on multiple assignments and do not provide focussed time to each case to ensure timely completion
- A delayed arbitration award is loaded against the timeframes in which an Investor operates (most funds have a total fund life of 8-10 years) leading to Investors compromising early in the process

Arbitration/ litigation are still seen as legally very weak procedures in India. Often, they are seen as pressure points rather than a mechanism to get an award in favour of the investor. Arbitration is truly effective if the promoter/ company has specific constraints that make it in their interest to seek an out of court conclusion of the arbitration/ litigation.

...and what may change?

In pursuance of its ease of doing business' agenda and an overall attempt to attract investors, the Government plans to enact the Commercial Divisions Act and Amendment to Arbitration and Conciliation Bill, 2015 (pending in Parliament). These legislations address key procedural concerns and have the potential to transform the arbitration/ commercial dispute resolution process in India. Post passage, interpretation/implementation will be key to their effectiveness.

Key amendments in The Arbitration and Conciliation Bill, 2015

In order to ensure neutrality of arbitrators, a potential arbitrator shall disclose in writing about existence of any relationship or interest of any kind, which is likely to give rise to justifiable doubts.

Requirement that the Arbitral Tribunal shall make its award within a period of 12 months. Parties may extend such period up to six months and thereafter, it can only be extended by the Court, on sufficient cause. The Court while extending the period may also order reduction of fees of arbitrator(s) not exceeding five percent for each month of delay

Provide a fast track procedure for conducting arbitration through mutual agreement of Parties to the dispute. Award in such cases shall be given within a period of six months.

Proposal to restrict the term 'Public Policy of India" as grounds to challenge of an arbitral award, by explaining that only where making of award was induced by corruption, or it is in contravention with the fundamental policy of Indian Law or is in conflict with the most basic notions of morality or justice, the award shall be treated as against the Public Policy of India.

A new provision to provide that application to challenge the award is to be disposed of by the Court within one year.

The award can only be stayed where the Court passes any specific order on an application filed by the party.

An application for appointment of an Arbitrator shall be disposed of by the High Court or Supreme Court as expeditiously as possible and an endeavour should be made to dispose of the matter within 60 days.

Comprehensive provisions for costs regime to avoid frivolous and meritless litigation/arbitration.

Empowering the Arbitral tribunal to grant all kinds of interim measures which the Court is empowered to grant and such order shall be enforceable in the same manner as if it is an order of Court.

Commercial Divisions Act/ Bill

The Commercial Divisions Act introduces a commercial division in every high court having original jurisdiction (i.e. Madras, Delhi, Bombay, Calcutta and Himachal Pradesh) and commercial courts in districts (to be mutually agreed by Central/ State government and Chief Justice of the concerned High Court). These specialised courts will resolve all "commercial" disputes (widely defined) of value exceeding Rs. 10mn.

These disputes will be heard by judges who not only have a background in commercial laws but will also receive special training in this area.

The Bill provides for a fast track mechanism with stringent timelines. It introduces the concept of a case management conference wherein a procedural order is passed prior to trial, setting out a time table (including time-bound oral arguments/ written arguments) that has to be strictly adhered to. The court is given powers to ensure strict compliance and is also required to deliver its judgment within a period of 90 days.

The Bill adopts the "carrot and stick" approach. It offers "carrots" for compliance and provides courts the power to wield the "stick" in case of delay by one of the parties. The Bill also makes mandatory the 'cost follow the event' regime, whereby, as a general rule, the party against whom the order/judgment is passed bears the entire cost of litigation, subject to exceptions where delaying parties, even if successful, have to bear part of the cost.

Is involving the media an option for PE Investors?

Going to the media is usually not considered a worthwhile option for PE Investors. Shareholder agreements typically carry confidentiality clauses that cannot be breached by parties.

Details in media of differences with an investee company is believed to reflects poorly on the quality of the investment made by the PE fund, negatively impacts ability to make future investments, impacts any future fundraising exercise and puts the fund/ key individuals at risk of reverse pressure tactics being applied.

Box 3: What are PE Investors now doing to proactively address potential problems

The pendulum has swung back towards tighter Shareholder Agreement terms from the period of 2005-2011 when competitive conditions led to PE investors agreeing to lax terms that did not stand the test of tough economic conditions.

The financial audit is now being undertaken in far greater depth with particular focus on aspects such as confirming cash on books, tracing key transactions through the accounts and undertaking a deep dive into related party transactions.

Forensic audits to check the background of the promoter, any cash leakages, criminal cases etc are being made part of the standard due diligence process prior to investment.

Incorporating upfront terms in the SHA that incentivise the promoter to act in a positive manner (e.g. PE sharing upside beyond threshold returns at stage of exit) or oblige the promoter to act to prevent penal provisions (e.g. hold pledged shares of the promoter in an escrow against convertible debt instead of depending on their undertaking to provide an exit).

Eschewing certain structures that tested the spirit of Indian law as investee companies successfully argued against adhering to such terms (e.g. the Put option provided to investors by Financial Technologies if the proposed IPO of MCX did not take place within a specified timeframe could not be exercised by the investors)

Some PE investors are reviewing whether it is better to appoint independents to represents the PE fund on the board of an investee company (instead of a member of the PE fund), especially in the context of the new Act, as it reduces conflict situations that have been used against them by investee companies.

Are too many regulatory cooks playing spoilsport?

Company Law Board (CLB)/ National Company Law Tribunal (NCLT)

- The Act provides investors significant leverage with the NCLT proposed to subsume a significant part of the roles of CLB/ BIFR and High Courts for matters relating to the Act.
- The Company Law Board (CLB) has been the key recourse for Investors, especially in unlisted entities. However, CLB procedures remain slow, CLB personnel often do not appreciate the finer aspects of agreements/ valuation and are sometimes open to crooked practices.
- Moreover, NCLT is yet to be constituted and there is significant concern on its ability to resolve disputes in a timely manner. In addition, the powers/ role of CLB and NCLT have not been clearly delineated.
- The recent dilution of approval required from minority shareholders for Related Party Transactions (RPT) under the Act is cause for further concern.

Securities and Exchange Board of India (SEBI)

- While SEBI has taken many steps to improve corporate governance, it is essentially focused on listed companies and matters involving public funds. SEBI is focused on violations of law rather than contentious matters of fairness (which is often the case in matters of RPT).
- The system of SCORES set up by SEBI (which allows an investor to record and follows his complaints using SEBI platform) does not follow through to act on inadequate responses or unfair actions taken by a company.
- PE investments in unlisted entities are typically not seen as a SEBI responsibility.

Central Bureau of Investigation (CBI)/ Economic Offences Wing (EOW)

- The CBI/ Economic Offences Wing (EOW) can typically be invoked where "public" funds are involved. They are typically overburdened and unless a regulatory body like a Court is driving the process, investigations tend to get significantly delayed.
- An added concern is that these entities tend to view all stakeholders with eyes of "suspicion" and this tends to put the entire business of the investor under regulatory scrutiny.

Serious Fraud Investigation Office (SFIO)

- As per the Charter and Responsibilities of SFIO, it will take up investigation of only such cases which are characterized by complexity and having inter-departmental and multi-disciplinary ramifications', substantial involvement of public interest judged by size, either in terms of monetary misappropriation or in terms of persons affected and the possibility of investigation leading to or contributing towards a clear improvement in systems, laws and procedures. SFIO effectively requires involvement of "public" funds for it to consider the Investor complaint.
- In practical terms the effectiveness of the organisation is untested without significant successful prosecutions to date.

Conclusion

During the last few years shareholders have become more proactive in seeking redressal of corporate governance transgressions. This has been strongly supported by changes in regulation (such as approval by majority of minority shareholders on related party transactions under the Act) and a tighter corporate governance framework developed by SEBI. In a connected, social network driven environment companies have increasingly seen the benefit of good corporate citizenship and the adverse impact of corporate governance issues on their brand, financial performance and valuations.

Prosecution of companies and individuals that undertake corporate malfeasance however remains a challenge in India. Regulatory bodies tend to proceed on investigations/ prosecutions only when the matter is in the media (a fickle audience) leading to considerable pressure to act or when they are being pushed by the Courts (e.g. Sahara Group cases). Even in high priority cases the timeline to conclude investigations and persecution of the perpetrators is significantly delayed which leads to public fatigue and media ennui.

On the other hand, investors in listed companies often do not have the bandwidth (with multiple investments) and the time horizon to follow up on ensuring investigations lead to their correct conclusion. It is often preferable for a public market investor to simply display their concern through an exit on the bourse leading to a self-inflicted fall in valuations that mainly hurts the investor and the company/ promoter to a limited extent. Similarly, PE Investors with a typical fund life of 8-10 years are disadvantaged vis-à-vis a promoter in getting fair redressal and often prefer to exit the investment with the best possible compromise.

The SEBI (Listing Obligations and Disclosure Requirements) Regulations notified on 2 September 2015 will provide some more information to investors to form an opinion on major transactions. Critically, this regulation provides SEBI the ability to directly regulate listed entities for enforcement of clause 49 and related clauses of the listing agreement unlike earlier when SEBI had to go through stock exchanges being a contract between the stock exchanges and issuer companies. The regulations came into effect from 1 December 2015.

The proposal to enact the Commercial Divisions Act and Amendment to Arbitration and Conciliation Bill, 2015 could significantly address concerns around the arbitration/ commercial dispute resolution process in India. Investors, however, need to guard against dilution of corporate governance norms in order to ensure "ease of doing business" for corporate India (e.g. allowing parties that are not interested in a resolution to vote on RPT matters along with minority investors under the modified Act).

Annexures

Annexure 1: List of resolutions that have recently been defeated by shareholders

S No.	Company	Meeting date	Resolution
1	Bharat Electronics Ltd.	3-Sep-15	Appointment of JR Krishna Rao as a Director
2	Camson Biotechnologies Ltd.	24-Sep-14	Declare dividend on equity shares
3	Coal India Ltd.	10-Sep-14	To appoint Dr. RN Trivedi as an Independent Director upto 30 October 2016
4	Coal India Ltd.	10-Sep-14	To reappoint Dr. Noor Mohammad as an Independent Director upto 18 December 2016
5	Coal India Ltd.	10-Sep-14	To reappoint Prof. Indranil Manna as an Independent Director upto 5 February 2017
6	Dhanlaxmi Bank Ltd.	20-Sep-14	Reappoint K. Vijayaraghavan as an Independent Director
7	Eros International Media Ltd.	28-Dec-14	Approval for entering into related party transactions in accordance with Section 188 of Companies Act 2013
8	Eros International Media Ltd.	28-Dec-14	Approval for making loan(s), giving guarantee(s), providing security(ies) and making investment(s) in other bodies corporate(s) upto Rs 10 bn in accordance with Section 186 of Companies Act 2013
9	Gayatri Projects Ltd.	28-Sep-15	Amendment to Articles of Association of the Company
10	Hindustan Zinc Ltd.	24-Jun-14	Reappointment of Deloitte Haskins & Sells as statutory auditors
11	Hindustan Zinc Ltd.	24-Jun-14	Reappointment of Ms. Shaukat Ara Tirmizi as director
12	Hindustan Zinc Ltd.	24-Jun-14	Reappointment of Rajib Sekhar Sahoo as director
13	I F C I Ltd.	27-Aug-14	Reappoint Omprakash Mishra as Independent Director
14	I L & F S Transportation Networks Ltd.	21-Aug-14	Issue of securities aggregating upto Rs.10.0 bn
15	McleodRussel India Ltd.	30-Sep-15	Approve remuneration payable to Aditya Khaitan, MD for a period of three years from 1 April 2014 as minimum remuneration in the event of loss or inadequacy of profit
16	Multi Commodity Exchange Of India Ltd.	29-Sep-15	Amend Articles of Association (AoA) to revise maximum board size to 15 members
17	Multi Commodity Exchange Of India Ltd.	29-Sep-15	Amend ESOP – 2008 Scheme of the company
18	Orient Refractories Ltd.	20-Sep-14	To create charge or mortgage on the company's assets
19	Panacea Biotec Ltd.	25-Sep-14	Enter into related party transactions with Pan Era Biotec Pvt. Ltd., an associate company, for upto Rs.3.2 bn
20	Repco Home Finance Ltd.	12-Sep-15	To approve related party transactions with Repco Bank up to Rs. 30.0 bn
21	Repco Home Finance Ltd.	12-Sep-15	To mortgage, create charge on all or any of the assets of the Company and further issue covenants for negative pledges/lien

S No.	Company	Meeting date	Resolution
22	Siemens Ltd.	17-Sep-14	Sale and transfer of the Company's Metals Technologies business as "going concern" and by way of a slump sale basis to Siemens Postal and Parcel Logistics Technologies Pvt. Ltd. (proposed to be renamed), a 100% subsidiary of Siemens AG, Germany w.e.f the close of business hours on 30 September 2014, pursuant to the provisions of Section 188 of the Companies Act 2013 and the rules framed thereunder
23	Steel Authority Of India Ltd.	23-Sep-14	Appointment of DK Mittal as Independent Director for a period of three years
24	Steel Authority Of India Ltd.	23-Sep-14	Appointment of RS Sharma as Independent Director for a period of three years
25	Tata Motors Ltd.	27-Jun-14	To approve and ratify the payment of excess remuneration paid to Karl Slym in view of inadequacy of profits for FY14
26	Tata Motors Ltd.	27-Jun-14	To approve the payment of minimum remuneration to Ravindra Pisharody in case of inadequacy of profits and ratification of the excess remuneration paid for FY14
27	Tata Motors Ltd.	27-Jun-14	To approve the payment of minimum remuneration to Satish Borwankar in case of inadequacy of profits and ratification of the excess remuneration paid for FY14
28	United Spirits Ltd.	26-Nov-14	To enter into distribution agreement, licence for manufacture and sale agreements and cost sharing agreement with certain Diageo subsidiaries
29	United Spirits Ltd.	28-Nov-14	Approval of advertising agreement dated 1 October 2013 between USL and Watson Limited
30	United Spirits Ltd.	28-Nov-14	Approval of agreements dated 30 September 2011 and 22 December 2011 respectively, between USL and UBHL requiring USL to buy from UBHL certain immovable properties
31	United Spirits Ltd.	28-Nov-14	Approval of aircraft services agreement dated 11 June 2013 between USL and UB Air Private Limited (UBAPL)
32	United Spirits Ltd.	28-Nov-14	Approval of contribution agreement dated 11 June 2013 between USL and Vittal Mallya Scientific Research Foundation (VMSRF)
33	United Spirits Ltd.	28-Nov-14	Approval of loan (aggregating Rs. 13.8bn) agreement dated 3 July 2013, between USL and United Breweries (Holdings) Limited (UBHL)
34	United Spirits Ltd.	28-Nov-14	Approval of properties call agreement dated 11 June 2013 between USL and PE Data Centre Resources Private Limited (PEDCRPL)
35	United Spirits Ltd.	28-Nov-14	Approval of services agreement (for property maintenance) dated 3 July 2013, between USL and Kingfisher Finvest India Limited
36	United Spirits Ltd.	28-Nov-14	Approval of sponsorship agreement dated 11 June 2013 between USL and United Mohun Bagan Football Team Private Limited (UMBFTPL)
37	United Spirits Ltd.	28-Nov-14	Approval of sponsorship agreement dated 11 June 2013 between USL and United Racing & Bloodstock Breeders Limited (URBBL)

Annexure 2: Corporate Governance in the listed space is driven by SEBI and the Companies Act

In 1999, SEBI constituted a Committee on Corporate Governance under the Chairmanship of Shri Kumar Mangalam Birla, to promote and raise the standard of corporate governance in respect of listed companies. SEBI incorporated the recommendations of the Committee by inserting Clause 49 in the Equity Listing Agreement. Since then a number of committees have been instituted by SEBI and the Government that have slowly raised the standard of disclosure and corporate governance amongst Indian corporates. Clause 49 of the Equity Listing Agreement consists of mandatory as well as non-mandatory provisions.

On 2 September 2015 SEBI notified the SEBI (Listing Obligations and Disclosure Requirements) Regulations 2015(Listing Regulations) for listed entities providing the framework of responsibility of companies/ Board towards its shareholders and aligning SEBI regulations with the Act. It also provides detailed guidelines to ensure adequate and timely disclosure of information on an ongoing basis in a structured format. The Listing Regulations defines events that listed companies need to disclose irrespective of materiality (Part A) and those than need disclosure based on materiality (Part B). The regulations also define the details that need to be provided while disclosing events and when the event needing disclosure can be said to have occurred for the purpose of disclosure. The regulations also require parity of information disclosure with any overseas stock exchange where the securities of the listed entity may be listed. The regulations came into effect from 1 December 2015.

These regulations now replace clause 49 and other related corporate governance clauses in the listing agreement (signed between stock exchanges and companies) with the regulations issued by SEBI. It gives SEBI direct access to regulate listed entities on matters of corporate governance unlike earlier when SEBI had to go through stock exchanges as the listing agreement was a contract between the stock exchanges and issuer companies.

Aside from the Listing Agreement, SEBI has taken other policy measures for ensuring better governance in listed companies including:

- Disclosure and open offer requirements, as required under SEBI (Substantial Acquisition of Shares and Takeover) Regulations, 2011 ("Takeover Regulations") and Clause 40B of the listing agreement.
- Disclosure of promoter pledged shares (both event-based and periodic), as mandated by Regulation 31 of the Takeover Regulations.
- Compulsory dematerialization of promoter holdings to improve transparency in the dealings of shares by promoters, as mandated by SEBI Circular dated June 17, 2011, bearing reference no. Cir/ISD/ 3/2011.
- Maintenance of minimum public shareholding (25%), as required under the provisions of Regulation 19(2)(b) and Regulation 19(A) of the Securities Contract (Regulation) Rules, 1957.

The Act has ushered a requirement of better corporate governance in some key areas enumerated below:

- Related party transactions require approval by majority of minority shareholders
- Requirement to constitute Remuneration and Nomination committee and Stakeholders Grievances Committee for companies meeting specific size criteria
- Granting of more powers to Audit Committee
- Specific clause pertaining to duties of directors
- Mode of appointment of Independent Directors and their tenure

- Code of Conduct for Independent Directors
- Rotation of Auditors and restriction on Auditor's for providing non-audit services
- Enhancement of liability of Auditors
- Disclosure and approval of RPTs
- Mandatory Auditing Standards
- Enabling Shareholders Associations/Group of Shareholders for taking class action suits and reimbursement of the expenses out of Investor Education and Protection Fund*(currently not notified)*
- Constitution of National Financial Reporting Authority, an independent body to take action against the Auditors in case of professional misconduct*(currently not notified)*
- Requirement to spend on CSR activities

The key points relating to these key governance drivers in the Act are provided in Annexure 3 and we would strongly recommend a review by the reader for a deeper understanding of relevant areas.

Annexure 3: Key corporate governance related clauses in the Act

Related party transactions (RPTs)	Section 188 of the Companies Act, 2013 read with Rule 15 of the Companies (Meetings of Board and its Powers) Rules, 2014 mandates that a company must obtain the prior approval of the majority of the minority shareholders for the purpose of:
	• entering into a contract or arrangement with any related party where such company has a paid-up share capital of Rs.100mn or more; or
	• entering into any of the following transactions with a related party:
	  • contracts/arrangements involving the following:
	  ○ sale, purchase or supply of goods or materials exceeding 10% of the turnover of the company or Rupees one thousand mn, whichever is lower;
	  ○ selling or otherwise disposing of or buying property exceeding 10% of the net worth of the company or Rs.1000 mn, whichever is lower;
	  ○ leasing of property exceeding 10% of the net worth of the company or 10% of the turnover of the company or Rs.1000 mn, whichever is lower;
	  ○ availing or rendering of services exceeding 10% of the turnover of the company or Rs.500 mn, whichever is lower;
	  • appointment to any office or place of profit in the company, its subsidiary or associate company at a monthly remuneration exceeding Rs.250,000; or
	  • payment of remuneration for underwriting the subscription of any securities or derivatives of the company exceeding 1% of the net worth of the company.

Requirement to constitute remuneration and nomination committee and Stakeholders Grievances Committee	Section 178 of the Act read with Rule 6 of the Companies (Meetings of Board and its Powers) Rules, 2014 directs the Board of every listed company and every company belonging to any of the following classes of companies to constitute a Nomination and Remuneration Committee: • public companies with a paid up capital of Rs.100 mn or more; • public companies having turnover of Rs.1000 mn or more; • public companies, having in aggregate, outstanding loans or borrowings or debentures or deposits exceeding Rs.500 mn or more. The role of the Nomination and Remuneration Committee among other responsibilities is to formulate a policy for the directors, key managerial personnel and other employees of the company. Section 178 of the Act also directs the Board of every company having more than 1000 shareholders, debenture-holders, deposit-holders and other security holders to constitute a Stakeholders Relationship Committee. The role of the Stakeholders Relationship Committee is to consider and resolve the grievances of the security holders of the company.
Establishment of vigil mechanism	Section 177 of the Act read with Rule 7 of the Companies (Meetings of Board and its Powers) Rules, 2014 mandates that every listed company and every company belonging to any of the following classes of

	companies is required to establish a vigil mechanism to enable the directors and employees of the company to report their genuine concerns or grievances: • companies which accept deposits from the public; • companies which have borrowed money from banks and public financial institutions in excess of Rs.500 mn.
Granting of more powers to audit committee	Section 177 of the Act stipulates the powers and responsibilities of the Audit Committee which, *inter alia*, include: • recommending the appointment, remuneration and terms of appointment of auditors of the company; • reviewing and monitoring the auditor's independence and performance, and effectiveness of the audit process; • scrutinizing inter-corporate loans and investments; • evaluating the internal financial controls and risk management systems; • monitoring the end use of funds raised through public offers and related matters. The Audit Committee has also been conferred with the authority to investigate into any matter in relation to the aforementioned powers and responsibilities or referred to it by the Board and for this purpose, it is empowered to obtain professional advice from external sources and have full access to information contained in the records of the company.
Specific clause pertaining to duties of directors	The Act has imposed a number of duties and responsibilities on the directors which, inter alia, include the following: • a director must act in good faith and in the best interests of the company, its objects, its employees, its shareholders and the community; • a director must exercise his duties with due and reasonable care, skill and diligence; • a director must refrain from being involved in a situation in which he may have direct or indirect interest that conflicts, or possibly may conflict, with the interest of the company; • a director must disclose his concern or interest in any company, body corporate, firm, or other association of individuals; • a director must refrain from being involved in any forward dealings in the securities of the company, or its holding, subsidiary or associate company. Further, Section 134 of the Act requires the Board to prepare a Directors' Responsibility Statement stating, inter alia, that appropriate accounting policies and adequate internal financial controls had been adopted in the preparation of the annual accounts of the company.
Mode of appointment of Independent Directors and their tenure	Section 149 of the Act requires every listed company to have at least one-third of the total number of directors as independent directors. An independent director can hold office for a term up to 5 consecutive years, and will be eligible for reappointment with the prior approval of more than 75% of the shareholders Section 150 of the Act provides that an independent director can be selected from a data bank maintained by anybody, institute or association, notified by the Central Government, having expertise in

	creation and maintenance of such data bank. However, it is the responsibility of the company making the appointment to exercise due diligence before selecting a person from such data bank as an independent director. Such appointment is required to be approved by the shareholders in a general meeting.
Code of Conduct for Independent Directors	Section 149 of the Act requires independent directors to adhere to the standards of professional conduct stipulated in Schedule IV of the Act.
Rotation of Auditors and restriction on Auditor's for providing non-audit services	Section 139 of the Act mandates that every company is required, at the first AGM, to appoint an individual or a firm as an auditor, to hold office from the conclusion of that meeting till the conclusion of its sixth AGM and thereafter, till the conclusion of every sixth AGM, subject to the ratification of such appointment by the members. However, a listed company or a company belonging to any of the following classes of companies cannot appoint or re-appoint an individual as an auditor for more than 1 term of 5 consecutive years and an audit firm as an auditor for more than 2 terms of 5 consecutive years: • unlisted public companies having paid up share capital of Rs.100 mn or more; • private limited companies having paid up share capital of Rs.200 mn or more; • companies (excluding one person companies and small companies) having paid up share capital not exceeding the threshold limits mentioned in (a) and (b) above, but having public borrowings from financial institutions, banks or public deposits of Rs.500 mn or more. Rule 6 of the Companies (Audit and Auditors) Rules, 2014 directs the Board to consider the matter of rotation of auditors and recommend, or where a company is required to constitute an Audit Committee, such Audit Committee must recommend to the Board, the name of an individual auditor or of an audit firm who may replace the incumbent auditor on the expiry of the term of such incumbent auditor. Section 144 of the Act restricts an auditor from rendering, directly or indirectly, the following services to the company or its holding or subsidiary company, namely: • accounting and book keeping services; • internal audit; • design and implementation of any financial information system; • actuarial services; • investment advisory services; • investment banking services; • rendering of outsourced financial services; • management services.
Enhancement of liability of Auditors	Section 143 of the Act requires an auditor to make a report to the members of the company on the accounts and financial statements of the company examined by him. The auditor must comply with the auditing standards.

	If the auditor of a company has reason to believe that an offence involving fraud is being or has been committed against the company by the officers or employees of the company, he must report the same to the Central Government immediately but not later than 60 days of his knowledge. If the auditor fails to comply with this mandate, he shall be punishable with fine.
Disclosure and approval of RPTs	Section 188 of the Act read with Rule 15 of the Companies (Meetings of Board and its Powers) Rules, 2014 mandates that a company must obtain the prior approval of the majority of the shareholders for the purpose of entering into any stipulated related party transaction. Section 189 of the Act read with Rule 16 of the Companies (Meetings of Board and its Powers) Rules, 2014 mandates that every company must maintain one or more registers containing particulars of the following: • companies or bodies corporate, firms or other association of individuals, in which any director has any concern or interest, except in cases where such director himself or together with any other director does not hold more than 2% of the paid-up share capital of any such company or body corporate; • contracts or arrangements with a body corporate, firm or other entity, in which any director is, directly or indirectly, concerned or interested, where such director himself or in association with any other director, holds more than 2% of the shareholding of that body corporate, or is a promoter, manager, CEO of that body corporate or is a partner, owner or member, as the case may be, in such firm or other entity; and • stipulated related party transactions.
Mandatory Auditing Standards	Section 143 of the Act authorizes the Central Government to prescribe the standards of auditing or any addendum thereto, as recommended by the Institute of Chartered Accountants of India, in consultation with and after examination of the recommendations made by the National Financial Reporting Authority. However, until any auditing standards are notified by the Central Government, any standard or standards of auditing specified by the Institute of Chartered Accountants of India will be deemed to be the mandatory auditing standards.
Enabling Shareholders Associations /Group of Shareholders for taking class action suits and reimbursement of the expenses out of Investor Education and Protection Fund.	Section 245 of the Act empowers the prescribed number of members or depositors (to be notified), who are of the opinion that the management or conduct of the affairs of the company are being conducted in a manner prejudicial to the interests of the company or its members or depositors, to file an application before the NCLT on behalf of all members or depositors for seeking relief. Section 125 of the Act requires the Central Government to establish a fund called the Investor Education and Protection Fund and the moneys credited to such fund shall be utilized, among other things, for the reimbursement of the legal expenses incurred in pursuing class action suits.

	However, the aforesaid sections (Sections 245 and 125) of the Act have not been notified by the Central Government as of the date of publication of this consultative paper.
Constitution of National Financial Reporting Authority (NFRA), an independent body to take action against the Auditors in case of professional mass-conduct.	Section 132 of the Act empowers the Central Government to, constitute a National Financial Reporting Authority, which shall have the power, inter alia, to investigate, either *suo motu* or on a reference made to it by the Central Government, into the matters of professional or other misconduct committed by any member or firm of chartered accountants, registered under the Chartered Accountants Act, 1949, and where such professional or other misconduct is proved, to make an order for: • imposing monetary penalty; • debarring the member or the firm from practice. ***However, the aforesaid section (Section 132) of the Act has not been notified by the Central Government as of the date of publication of this consultative paper.***
Requirement to spend on CSR activities	Section 135 of the Act requires every company having net worth of Rs. 5000 mn or more, or turnover of Rs. 10000 mn or more or a net profit of Rs. 50 mn or more during any financial year to constitute a Corporate Social Responsibility Committee. The Corporate Social Responsibility Committee is required to: • formulate a Corporate Social Responsibility Policy indicating the activities to be undertaken by the company as specified in Schedule VII of the Act ; • recommend the amount of expenditure to be incurred on the aforementioned activities; and • monitor the Corporate Social Responsibility Policy of the company from time to time.

Annexure 4: Procedure to call an EGM by minority shareholders holding minimum 10% equity stake

- Section 100 of the Act read with Rule 17 of the Companies (Management and Administration) Rules, 2014 directs the Board to call an EGM at a requisition made by the shareholders of the company who hold, on the date of the receipt of such requisition, not less than 10% of the paid-up share capital of the company.
- Such minority shareholders should provide the requisition to call an EGM in writing or through electronic mode at least 21 days prior to the proposed date of the EGM.
- If the Board does not, within 21 days from the date of receipt of such requisition, proceed to call an EGM on a day not later than 45 days from the date of receipt of such requisition, the EGM can be called and held by the requisitionists themselves within a period of 3 months from the date of the requisition.
- Such meeting by the requisitionists will be called and held in the same manner in which the meeting is called and held by the Board.
- Any reasonable expenses incurred by the requisitionists for this purpose are to be reimbursed to the requisitionists by the company and the sums so paid are to be deducted from any fee or other remuneration payable to such of the directors who were in default in calling the EGM.

Annexure 5: Procedure to approach SEBI u/s 11 of the SEBI Act

While there is no specific procedure for approaching SEBI, it has a dedicated department viz., Office of Investor Assistance and Education to receive investor grievances and to provide assistance to investors by way of education.

- Grievances against listed company are taken up with the respective listed company and are continuously monitored.
- Grievances pertaining to stock brokers and depository participants are taken up with respective stock exchange and depository for redressal and monitored by SEBI through periodic reports obtained from them.
- Grievances pertaining to other intermediaries are taken up with them directly for redressal and are continuously monitored by SEBI.

SEBI also has a separate department to look into market irregularities. If any irregularities are found in trading in shares or manipulation in price or violation of Insider Trading regulations, the same can be reported to SEBI.

SEBI Monitoring Mechanism (SCORES)

The monitoring of investor complaints is managed through the SEBI Complaints Redress System or SCORES.

SCORES is a web based centralized grievance redress system of SEBI. SCORES enables investors to lodge and follow up their complaints and track the status of redressal of such complaints online from the above website from anywhere. This enables the market intermediaries and listed companies to receive the complaints online from investors, redress such complaints and report redressal online. All the activities starting from lodging of a complaint till its closure by SEBI is online in an automated environment and the complainant can view the status of his complaint online.

Annexure 6: How to approach CLB or NCLT

Sections 397 and 398 of the 1956 Act currently provide recourse to minority shareholders against oppression or mismanagement.

Under the new Act shareholders holding not less than one tenth of the issued share capital of the company, or shareholders not numbering less than a hundred, are permitted to approach the National Company Law Tribunal (NCLT) for relief in a case of mismanagement or oppression, which would include a situation where the affairs of the company are being carried out in a manner oppressive to a specific shareholder or class of shareholders or prejudicial to public interest.

The Central Government may waive this threshold in cases where it feels that such waiver would be just and equitable.

In the event that the NCLT finds that the grievance of the applicants is justified, it is empowered to pass wide-ranging orders to end the mismanagement/oppression complained which could include *inter alia* orders providing for:

- The regulation of the affairs of the company in future;
- The purchase of shares or interests of the shareholders or restrictions on the transfer and allotment of shares;
- The termination, setting aside or modification of any agreement between the company and its managing director, directors or manager;
- The termination, setting aside or modification of any agreement between the company and any other person (after providing due notice and obtaining the consent of the party concerned);
- The setting aside of any transfer, delivery of goods, payment, execution or other act relating to property, made or done by or against the company within three months prior to the date of the complaint, if the same would amount to a fraudulent preference;
- The removal of any managing director, directors or manager;
- The recovery of any undue gain made by any managing director, directors or manager;
- The imposition of costs as deemed fit by the Tribunal; and
- Any other matter that the Tribunal deems just and equitable.

The Act contains similar provisions with respect to reliefs against mismanagement and minority oppression with the important distinction that the NCLT itself (as opposed to the Central Government) has the right to relax the thresholds for being eligible to file a complaint. This could potentially make the application process easier for minority shareholders who do not meet the 10%/hundred shareholder threshold and improve corporate governance. However, the provisions of the Act in respect to relief against mismanagement and oppression have not yet been notified and the provisions of the 1956 Act (as described above) continue to remain in force.

As evidence by the wide ranging powers of the NCLT to set matters right, the right to approach the courts for relief against mismanagement and oppression is a powerful remedy in the hands of minority shareholders, which if utilized effectively, can act as an important safeguard against majority abuse. Whilst strategic investors protect themselves by also obtaining additional rights via contractual arrangements with the company and the promoters (through shareholders agreements and the like), financial investors may find it helpful to bear the significance of the 10% threshold in mind whilst considering potential investments in future.

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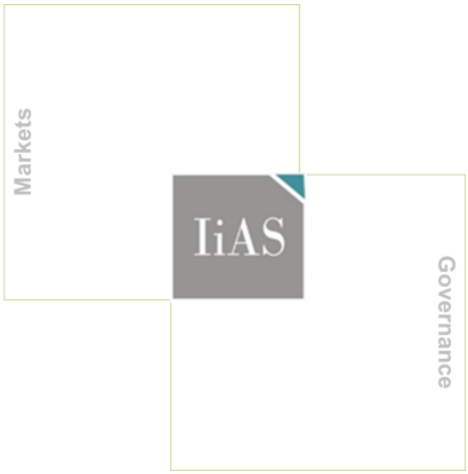

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