
THE EMERGENCE OF SHAREHOLDER ACTIVISM AND THE BREAKDOWN OF CORPORATE GOVERNANCE, PARTICULARLY IN INDIA

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ABSTRACT

Particularly in India, the growth of shareholder activism has become a powerful factor in changing corporate governance. The historical development, legal context, and effects of shareholder activism on corporate governance are all examined in this essay. The paper illustrates how activism has improved openness, accountability, and sustainability in Indian firms by looking at significant cases like the Tata Sons v. Cyrus Mistry case and the function of institutional investors. The difficulties that come with shareholder activism are also covered in the study, such as the possibility of aggressive strategies and short-termism. The report offers recommendations for enhancing the legal environment, encouraging positive participation, and incorporating Environmental, Social, and Governance (ESG) factors into corporate governance. In addition to offering suggestions for promoting a more just and sustainable business environment, the research attempts to give a thorough understanding of the contribution that shareholder activism makes to better corporate governance in India.

Keywords: Shareholder Activism, Corporate Governance, Participation, Legal Environment, ESG etc.

RESEARCH METHODOLOGY

Using secondary sources including academic journals, case studies, court records, and reports from regulatory organizations like the Securities and Exchange Board of India (SEBI), this study uses a qualitative methodology. An in-depth examination of the influence of shareholder activism on corporate governance is made possible by the use of a case study approach to investigate notable cases of activism in India. A study of the legal framework controlling shareholder activism in India is also included in the research, with an emphasis on important rules and changes.

RESEARCH QUESTIONS

- What are the main causes of the rise in shareholder activism in India, and how has it changed over time?
- How has shareholder activism affected corporate governance in India, and what is the legal structure guiding it?
- In what ways does shareholder activism affect corporate governance's sustainability, accountability and transparency?
- What obstacle does shareholder activism present, and how may they be overcome?
- Which Indian shareholder activism cases are the most notable, and what effect they had on corporate governance?

OBJECTIVE OF RESEARCH

This study's main goal is to investigate how shareholder activism has developed in India and how it affects corporate governance. The paper intends to offer a thorough examination of the legislative framework controlling shareholder activism, look at significant court decisions, and evaluate the prospects and problems related to this phenomena. Additionally, the study aims to provide suggestions for enhancing corporate governance via more successful shareholder involvement.

SIGNIFICANCE OF THE STUDY

The growing significance of shareholder activism in improving corporate governance in India is addressed in this paper, which makes it noteworthy. Given the growing emphasis on global issues including accountability, transparency, and environmental, social, and governance (ESG) concerns, it is imperative that politicians and corporate practitioners comprehend the function of shareholder activism. The results of this study will add to the body of knowledge already available on corporate governance and offer helpful advice for enhancing governance procedures in Indian businesses.

INTRODUCTION

Shareholder Activism and Corporate Governance: An Overview

Any corporation's ability to operate depends on its corporate governance, which is a set of policies and procedures that govern how businesses are run. Using shareholder stakes to influence a company's choices, or shareholder activism, has become an essential component of maintaining strong and transparent corporate governance. This relationship is especially important in India, where regulatory changes and economic liberalization have given shareholders more authority to participate actively in corporate governance.¹

HISTORY OF THE EVOLUTION OF CORPORATE GOVERNANCE AND SHAREHOLDER ACTIVISM

Corporate Governance: A Historical Perspective²

The necessity to resolve the division of ownership and control in firms has led to a substantial evolution in corporate governance during the past century. The development of governance measures aimed at aligning the interests of shareholders and management was prompted by the introduction of agency theory, which highlighted the inherent tension between the two groups.

¹ Neeraj Grover, Shareholder activism. Will the Indian landscape change? Deccan Herald, 2020. <https://www.deccanherald.com/opinion/panorama/shareholder-activism-will-the-indian-landscape-change850413.html>. (1843) 2 Hare 461, 67 ER 189.

² Brian R. Cheffins, The History of Corporate Governance, (Oct. 21, 2024, 11:00 AM), https://www.ecgi.global/sites/default/files/working_papers/documents/SSRN-id1975404.pdf

In addition to domestic economic and legal developments, global trends have impacted the evolution of corporate governance in India.

The Rise of Shareholder Activism

The increased awareness of the need for improved accountability and transparency in corporate governance, along with the growing influence of institutional investors, are the main causes of the growth in shareholder activism. The 1980s saw a rise in shareholder activism in the United States due to leveraged buyouts and hostile takeovers. Early in the new millennium, legal changes, financial market expansion, and economic liberalization all contributed to the rise of shareholder activism in India.

WHY SHAREHOLDER ACTIVISM CAME INTO PLAY

The Need for Enhanced Accountability and Transparency

The previous corporate governance model frequently fell short of safeguarding shareholders' interests, especially those of minority shareholders. The mismatch in interests between shareholders and management gave rise to shareholder activism as a means of guaranteeing the accountability and transparency of corporate governance processes. A greater effort was made by shareholders, especially institutional investors, to keep an eye on management and hold them responsible for their choices.³

The Influence of Institutional Investors

With their enormous corporate holdings, institutional investors have been a major factor in the growth of shareholder activism. Due to their involvement, corporate governance procedures are being examined more closely, and demands for accountability and transparency have grown. This tendency has been further encouraged by investors' increasing emphasis on ESG issues and their desire for corporate operations to be more in line with wider social and environmental objectives.

³ O.P. Khaitan & Co., Shareholder Activism in India, (Oct. 27, 2024, 12:10 PM), <https://www.advoc.com/news/shareholderindia>

LEGAL FRAMEWORK GOVERNING SHAREHOLDER ACTIVISM IN INDIA⁴

Regulatory Reforms and SEBI's Role

The SEBI regulations and the Companies Act of 2013 have formed the legal framework that governs shareholder activism in India⁵. For example, listed firms are required by the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 to disclose material events, guaranteeing shareholders' access to timely information. In order to defend shareholder interests, the Companies Act of 2013 also included measures including class-action lawsuits and the nomination of independent directors.

Proxy Voting and E-Voting Mechanisms

The implementation of electronic voting and proxy voting has additionally enabled shareholder activism in India. By enabling participation in decision-making processes even in the absence of physical attendance at general meetings, these techniques augment shareholders' capacity to impact corporate governance.

Recent Amendments and the Role of Institutional Investors

The recent modifications to the SEBI (Substantial Acquisition of Shares and Takeovers) and SEBI (Prohibition of Insider Trading) regulations, among others, have significantly influenced shareholder activism in India. The institutional investor community's role in encouraging shareholder activism has been reinforced with the implementation of SEBI's Stewardship Code in 2019.

LANDMARK INSTANCES OF SHAREHOLDER ACTIVISM IN INDIA

Tata Sons vs. Cyrus Mistry⁶

One of the biggest examples of shareholder activism in India is the conflict between Tata Sons

⁴ Karan Anand & Bhaskar Vishwajeet, Indian Shareholder Activism: Approaching a Turning Point?, (Oct. 26, 2024, 4:50 PM), [https://indiacorplaw.in/2024/05/indian-shareholder-activism-approaching-a-turning-point.html#:~:text=The%20Companies%20Act%2C%202013%20\(%E2%80%9C,shareholders%20against%20oppression%20and%20mismanagement](https://indiacorplaw.in/2024/05/indian-shareholder-activism-approaching-a-turning-point.html#:~:text=The%20Companies%20Act%2C%202013%20(%E2%80%9C,shareholders%20against%20oppression%20and%20mismanagement).

⁵ Khaitan & Co., The legal and regulatory framework surrounding shareholder activism in India, (Oct. 26, 2024, 5:30 PM), <https://www.lexology.com/library/detail.aspx?g=f3ff1c1c-d0b8-4d94-9370-771f0c2590a3>

⁶ Tata Consultancy Services Limited v. Cyrus Investments Private Limited and Ors., 2021 SC 184. Civil Appeal Nos. 440-441, 13-14, 442-443, 19-20, 444-445, 448-449, 263-264 and 1802 of 2020.

and its previous chairman, Cyrus Mistry. The case emphasized the significance of shareholder rights and transparency while bringing attention to corporate governance flaws within the Tata Group. The judicial struggle established a precedent for future activism in India and highlighted the significance of minority shareholders in contesting board decisions.

Infosys and the NR Narayana Murthy Controversy⁷

The board and management of Infosys were openly chastised in 2017 by the company's founder, NR Narayana Murthy, for their choices on acquisitions and CEO pay. Because of Murthy's activity, the CEO and a number of board members resigned, highlighting the ability of individual shareholders to affect corporate governance.

The ICICI Bank Case⁸

The 2018 ICICI Bank case demonstrated the increasing power of institutional investors in India as they called for an impartial inquiry into claims of a conflict of interest involving the CEO. The case showed that these investors were prepared to hold management responsible for shortcomings in corporate governance.

TYPES OF SHAREHOLDER ACTIVISM⁹

Proxy Battles

In proxy conflicts, shareholders try to influence other shareholders to vote in favor of their proposed changes in an effort to take over the company. These conflicts usually center on changing out board members or rejecting resolutions that management has offered.

Public Campaigns

Investors may utilize public campaigns to express dissatisfaction with a company's procedures, using public forums and the media to put pressure on management to alter its ways. Although

⁷ Srimoyee Chowdhury, Narayana Murthy speaks out on controversy over his '70-hour week' remark, (Sep. 01, 2024, 3:30 PM), <https://www.indiatoday.in/trending-news/story/narayana-murthy-speaks-out-on-controversy-over-his-70-hour-week-remark-2484623-2024-01-05?onetap=true>

⁸ Chanda Kochar v. ICICI Bank, 2023:BHC-OS:3853-DB

⁹ Corporate Finance Institute, Activist Shareholder, (Sep. 01, 2024, 3:40 PM), <https://corporatefinanceinstitute.com/resources/equities/activist-shareholder/>

this strategy can be useful in increasing awareness, if it is not handled appropriately, it could potentially harm the company's reputation.

Litigation

Another type of shareholder activism is litigation, in which protesting corporate actions or seeking remedies for grievances are done through legal action. Shareholders frequently utilize class-action lawsuits and derivative proceedings as legal instruments to address problems like fraud or poor management.

Engagement and Dialogue

In order to bring about reforms, constructive engagement entails shareholders holding private talks and negotiations with the board and management. This strategy seeks to resolve shareholder problems without going to court or involving the public.

IMPACT OF SHAREHOLDER ACTIVISM ON CORPORATE GOVERNANCE IN INDIA¹⁰

Enhancing Transparency and Accountability

In India, shareholder activism has greatly improved corporate governance's accountability and openness. Enhanced monitoring by stakeholders, especially institutional investors, has resulted in stronger governance procedures and increased transparency of data.

Strengthening Minority Shareholder Rights

Additionally, activism has been essential in defending minority shareholders' rights and making sure that management or majority shareholders do not ignore them. To safeguard minority shareholders and foster a more equal corporate climate, new laws and regulations have been introduced.

Driving ESG Initiatives

A new wave of shareholder activism centered on corporate responsibility and sustainability has

¹⁰ Ansh Mishra, Corporate Governance and Shareholder Activism in India, (Oct. 22, 2024, 12:45 PM), <https://aklegal.in/corporate-governance-and-shareholder-activism-in-india/>

emerged as a result of the growth of ESG concerns. Companies are under growing pressure from shareholders to implement greener policies, better labour practices, and higher governance requirements.

Challenges and Concerns

Notwithstanding the benefits of shareholder action, problems still exist. Confrontational methods have the potential to generate instability and divert management from business operations, and activist shareholders may place a higher priority on short-term rewards than long-term sustainability.

SUGGESTIONS AND RECOMMENDATIONS

Strengthening the Legal Framework

For shareholder activism to be more effective, the legal framework pertaining to corporate governance must be strengthened. This can entail strengthening voting procedures, imposing stricter disclosure regulations, and offering minority shareholders more protection.

Encouraging Institutional Investor Participation

One of the most important factors in encouraging shareholder activism is institutional investing. Companies can be held responsible for their governance practises if efforts such as SEBI's Stewardship Code are used to encourage increased involvement from these investors.

Promoting Constructive Engagement

Encouraging positive communication between management and shareholders helps resolve issues without the need for lawsuits or public spats. Establishing forums for communication and cooperation is crucial to promoting an atmosphere of corporate governance that is more accountable and transparent.

Integrating ESG Considerations

Companies should incorporate ESG factors into their corporate governance structures, given their significance. ESG integration is something that shareholders should keep pushing for, and regulators should offer standards to make sure businesses comply with these demands.

CONCLUDING REMARKS

Increased accountability, sustainability, and openness in corporate governance have been brought about by the surge in shareholder activism in India. Activism's influence over corporate governance will only increase as the law changes and shareholders gain more clout.

But striking a balance between empowering shareholders and making sure activism doesn't jeopardize the company's long-term interests is crucial. India can establish a more strong and equitable corporate governance environment that is beneficial to all stakeholders by fortifying the legislative framework, fostering constructive engagement, and increasing participation from institutional investors. Undoubtedly, the increasing increase of shareholder activism will continue to affect corporate governance in India, making it an important topic for policy creation and ongoing research.

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