

A Study on Role of Shareholder Activism in Economic Development of India

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Abstract: The genesis of shareholder activism in India can be traced back to early 2010 when SEBI came up with a mandatory requirement to disclose their voting policies as well as voting actions at their investee organizations on an annual basis. Clause 49 of listing agreement which is implemented by SEBI inculcate the essence of the new organizations act for greater participation of minority shareholders in taking racial decisions of the organizations, it also strengthens the role of independent directors serving on corporate boards and disclosure of detailed information about remuneration of directors and SEBI had put forward the responsibilities of audit committees. It is considered to be a set of dynamic efforts on the part of shareholders to change the behavior of organizations and governance rule. Proxy advisory which is regulated by SEBI has made immense contribution. The paper focuses on regulatory reforms towards shareholders, the influence of activist's shareholders on organizations and impact of share market on shareholders in India after the union budget which has hampered majority investors. Case study analysis is used to gather the data on shareholder activism

Keywords: *Shareholder Activism, Proxy Advisory Firm, Minority Shareholders*

I. INTRODUCTION

Activism firm involves the efforts of the shareholders to bring a desired change in the operations of the organizations or to influence the management in governing the organizations to protect the interest of stockholders. In India, Companies Act 2013 is the main source of law relating to shareholder activism by giving voting rights, appointing small directors, considering minority shareholders decisions in corporate governance etc.

Activists shareholders has increased in total capital deployed as well as number of campaign mounted. Approximately 65 billion dollars capital was deployed across 25 campaigns by 130 activists. These figures represent a modest increase in figures from the previous year. It also increases corporate efficiency by targeting well performed large cap firms with the plans to increase shareholder value. All these constitute overall economic development of our country. On other hand share market is showing a downward trend which has affected the majority shareholders. Activist shareholders are making their efforts to retain public shareholders as these people are losing their investment and rather not ready to take risk for further investment.

II. LITERATURE REVIEW

In case of Raymond Ltd, it was examined that organizations had proposed to sell property to its chairman at a price which is relatively lesser than market value. The organizations gave a explanatory statement that this would result a loss for organization. 99% institutional investors and 92.35% non-institutional shareholders votes were against this proposal. The result was proposal failed to pass since total of 97.67% votes

were against the resolution.

Alembic Pharmaceuticals Ltd fails to appoint a small shareholders director as it received a proposal from 1000 plus minority shareholders under a portfolio manager Unifi Capital Private Ltd. It was investigated and organizations rejected the request stating reason that it did not have any meaningful logic. The organizations did not consider the proposal of minority shareholders.

It was examined in case of MRO Tex Ltd that public shareholder requested for a postal ballot where the requisitionist proposed to appoint him as a non-executive director as he holds 20% of equity shares of a organizations. The reason behind this was requisitionist had under taken continuous transaction for developing a land parcel owned by the organizations. The agreement was signed with unrelated party who will be a new promoter of organizations. Agreement was not in favor of the minority shareholders. The proposal failed since all the promoters were voted against it and restricted it from getting a simple majority vote.

It was analyzed that two investors file a case against Religare enterprises Ltd. First one was filed by IDBI Trusteeship Service Ltd in Bombay High Court and the other is by its shareholders India Horizon fund Ltd in New Delhi bench of National Company Law Tribunal. The suits are against the proposal by organizations for investing Rs.500 crore in a loss making 100% subsidiary Religare Capital Market Ltd. 99.95% institutional investors voted against it. But the resolution was passed after considering the approval form promoters and institutional investors.

Promoters are also very important on the part of organization. It happened in case of Supreme Tex Mart where the members had a misunderstanding among themselves. The outcome of this case was requisitionist removed two promoter executive directors on the Board and appointed himself as Managing Director and family members as directors. The decision was failed as one promoter executive director and woman independent director resigned from the board.

It was analyzed in case of Maruti Suzuki, where organizations had asked for postal ballot from public shareholders to approve the setting up and operation of its new Gujarat plant by a wholly owned arm of Maruti Suzuki was a test case on shareholder activism in India. 89.75% of the shareholders who voted on the deal have approved the transaction where minority shareholders are being called to vote after the new Companies Act made it mandatory for listed firms to seek such special approval

III. RESEARCH METHODOLOGY

A. Objectives of the study

- To analyze the regulatory reforms of greater shareholders under Companies Act 2013

- b. To understand the influence of activists shareholders over companies
- c. To map the impact of share market on shareholders in India after the Union Budget 2019

B. Scope and Limitations of the study:

The study limits only to shareholder activism in India and it helps to understand the regulatory reforms under Companies Act 2013 and their influence on companies and to understand the share market which had a negative impact on majority shareholders. The information is purely gathered on secondary sources.

IV. ANALYSIS AND INTERPRETATION

A. Regulatory Reforms of Greater Shareholders under Companies Act 2013

Shareholder participation in India has been magnified by new capital market rules and Companies Act 2013. These regulations empowered the minority shareholders and now they can tell their opinion and more actively defend their interest. Share holder participation in the management of the organizations been enhanced by the following:

- a) **Electronic Voting:** Section 108 of Companies Act 2013, central government may prescribe the classes of companies and manner in which members may exercise his right to vote by electronic means. Companies can also provide video conferencing connectivity during the meeting in at least five locations in India. General meeting of organization are held at their registered office which is difficult for shareholder to cast their vote. E-voting has eliminated such hindrance and shareholders can also participate in decision making policy of organizations. In July, 2012 SEBI amended the listing agreement requiring large companies to provide electronic voting (e-voting) facility in respect of matters requiring postal ballot. According to this dispensation, top 500 listed companies on the Bombay Stock Exchange and National Stock Exchange now provide e-voting facility and this is quickly being extended by all listed companies.
- b) **Approval of related party transaction by minority shareholders:** Section 188 of Companies Act 2013 requires consent of BOD by passing a resolution for a organizations to enter into any contract or arrangement, BOD should report to shareholders along with the justification of entering into the contract. If organizations enters into any contract without passing any special resolution or without the consent of BOD or by shareholders at a meeting within three months from the date of the contract entered into such contract will be voidable at the option of the board and if the contract is with related party to any director or it is authorized by any other director, the director concerned shall indemnify the organizations against any loss incurred by it.
- c) **Shareholders Class Action Suit:** Section 245 of the Companies Act 2013 empower the members, depositors or any class of them can file an application before the Tribunal on behalf of the members or depositors, if they are of the opinion that the management or conduct of affairs of organizations are conducted in a manner which is unfavorable to members or depositors. Where the members or depositors seek any damages or compensation or demand any other suitable action from or against an audit firm, the liability shall be of the firm as well as of each partner who was involved in making any improper or

- d) **Participation of institutional investors:** Government of India & SEBI made greater efforts to encourage mutual funds in participating in corporate decision making. In 2010 SEBI has enacted a circular to mutual funds where it has to excise their voting rights in the investee organizations in a responsible manner. SEBI has also sent a circular that the asset management companies have to disclose their annual reports general policies regarding the excise of their votes in the listed companies.
- e) **Proxy advisor industry in India:** since 2010 the proxy advisory industry had gained a lot of prominence in India. It has publishes 100's of recommendations regarding corporate proposals relating to various listed companies in India. Their recommendation includes organizations proposals relating to appointment of Directors, auditors, and major corporate transactions such as mergers and take overs. The interest of minority shareholders is protected from the hands of majority shareholders and management of the organizations.
- f) **Mismanagement and oppression:** section 241 of Companies Act 2013 says that any member of organization including majority shareholders can file an application before a tribunal if the affairs of the organizations are being conducted in oppressive and pre judicial manner. If the central government comes to an conclusion that affairs of organizations are being conducted in a manner which is un favorable to public it may itself apply to the tribunal for an order.
- g) **Appointment of director elected by small shareholders:** section 151 of company's act 2013 requires that listed organizations should have 1 director elected by small shareholders according to the terms and conditions prescribed by central government. Small shareholders include a shareholder holding shares of a nominal value of not more than 20000 or such other sum as may be prescribed.

B. The influence of activist's shareholders on companies

Shareholders play an important role in decision making which will have a greater influence on companies. Sometimes management decisions and organizations' decisions does not go along with one another. Some of the pros and cons of the activist shareholders are discussed:

- a. **Controls management:** individuals or small investors do not have any contact with management because as they hold a small amount of shares which are called as outstanding stock. But activist investors have more influence as they purchase large quantities of stock and they are very powerful. They have all the rights to replace the existing boards. Activist often has the ability to hold management feet to fire and demand results. This in turn can make them work harder and cause them to try to find ways to enhance stakeholder value.
- b. **Innovative ideas from new faces:** large investor who has established a large position over time often has ideas about the utilization of organizations assets, improve operation or enhance shareholder value. But management may not be willing to accept new suggestions and ideas. If organizations accept such suggestions it will be an opportunity for inculcating such innovations
- c. **Demand for the share could perk up:** activists snap a large percentage of an organizations outstanding stock in a relatively short period of time. This makes the individuals

- to copy these activists by buying the stock as well in the hope of turning a tidy profit. This could push the stock price up and benefit common shareholders.
- d. Activists demand management: activists can sometime demand certain changes from existing management regarding change in board of directors or spin off the business or on competing with rivals etc. so it is forced to change the decisions of the management.
 - e. Selling could be an issue: activists may purchase large blocks of stock which increase the share price. But when the activists decide that it is a time to unload the shares it may logically place a significant amount of downward pressure on the share price.
 - f. Activist's acts according to themselves: activists firm often try to convince existing shareholders and the media to understand and act according to their agenda, but at the end of the day they may be acting according to them in their best interest. It would be wise for investors to keep this possibility in mind when listening to an activist agenda in the press.
 - g. Improper decisions in trading: many individual shareholders will be smarter than the average investor. They have extensive experience in trading in stock exchange. There is a belief that activist may have important industry contact and access to good research expertise. The strategy does not work in a positive way. In a current situation the share are over sold in a stock market as it is showing a downward trend and these strategies will not work out.
 - h. Activists may have a different investment horizon: investment horizon is the term used to describe the total length of time that an investor expects to hold a security or portfolio. In some cases many investors has to hold the securities for years together. On the other hand investor holds their stock for a long time they will win board seats and make the organizations to accept their agenda. Again the activists differ according to different investment horizon form the average investor. They should financially accept a loss on the position.
- e) Nearly 40% of the foreign portfolio investors in India are structured as all of them would end up paying steeply higher taxes.
 - f) A slowing income group and NBFC crises are primary reasons for current slowdown in automobile industry. It has drastically fallen to 24% in the month of august. This had a impact on the shareholders who hold block of shares.
 - g) Merger of PSU banks has again showed a downward trend in the bank nifty. According to analyst, the proposed merger with fresh recapitalization of Rs.55000 crore in the merged entries which has given a new life into the public sector banks hits by shrinking bottom line due to high non-performing assets. This has led to significant value erosion reflecting in their weak stock performance. Due to all these reasons the shares are oversold in the market and it has become a bearish trend. The activists shareholders could not take any decisions which helps to improve the performance of the organizations.

Due to slowdown of our growing economy Finance Minister Nirmala Sitharaman announced a some measures including scrapping surcharge on Foreign Portfolio Investors (FPI) and domestic market players and steps to improve the flow of loans and overall cash in the system, while promising easier rules and lower compliance burden on organizations. The minister also offered to review the surcharge on those with taxable income of over Rs.2 crore by 2022 and separate cell is set up to deal with tax issues of startups. All these have boosted FPI to increase their investments in our Indian stock market which helps in the economic growth of our country.

CONCLUSION

Indian companies need to give preference to small shareholders as it is analyzed in case studies that the minority shareholders are not taken into consideration. More institutional investors including the public sector institutional investors should engage actively with companies on routine and non-routine proposals. Since SEBI has protected the rights of shareholders as they have a right to take part in the management decisions. The main target of an activist shareholders are the organizations with strong cash flow, low dividend payout ratio, recent under performance or assets ripe for spinning off. The board should be actively aware of all these conditions and actively discussing them with management regardless of activist activity. Proxy advisory firm also give recommendations regarding corporate proposals and these firms are regulated by SEBI. On the other hand shares are been oversold in a stock market and showing a bearish trend even after the removal of surcharge where stock holders are not looking forward for any investments, no production, no consumption and the Gross Domestic Product (GDP) has forecasted to 6.2% for the year 2019.

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C. The impact of share market on shareholders

The Sensex has lost over 2000 points since the day of the budget announcement. It was surprising that it was supposed to be a progressive budget intended to put more money in the hands of the people and the effect was vice versa. The cause is not only because of union budget but the economic slowdown is happening throughout the world. The cause of fall in share market is due to:

- a) The first disappointment is increase in corporate dividend tax. There were strong expectations that the budget would cut tax ratio to 25% which was increased to 30%.
- b) The budget imposed 20% tax on buy back on the difference between buy back price and the issue price. This had an impact on dividend distribution tax. This tax may show a vertical slope on investors who invested recently.
- c) The proposal was to increase the public shareholding from 25% to 35%. But there will be huge supply of paper in market. When there is a large supply this would bring down the price of securities in turn which will have a greater impact on pressure on valuation of shares.
- d) The budget also imposed a higher surcharge of 25% on income above Rs.2 crore and 37% on income above Rs.5 crore. This higher surcharge on higher income group has freeze the shareholders income.

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