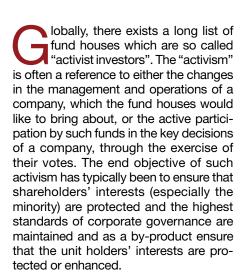
Mutual funds as responsible investors



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Current state of affairs

Apart from the odd example, India and Indian companies do not have a history of activist institutional investors and have not really tasted the sting of a fund's activist behaviour.

A notable example of institutional investor activism in India is the case of Satyam Computers Services. What most people remember about the infamous Satyam scandal is that the company initially shot into the news because of the failed acquisition of two companies run by the sons of the Satyam promoter (100% stake in Maytas Properties and 51% stake in Maytas Infrastructure), but the reasons for the failure of the acquisitions are often overlooked. After all Satyam was forced to stall its plans only because of the stiff opposition it faced from its institutional investors. If fund houses such as Templeton and SBI Mutual Fund had not opposed the acquisitions strongly, it is likely that the Satyam scandal would never have surfaced.

However, barring such examples, which are more the exception than the norm, institutional investor activism is a fairly recent trend in India, where managements have usually enjoyed the comfort of passive boards and investors. In developed jurisdictions by contrast, shareholder activism exercised by individual investors and the role of large institutional investors in ensuring adherence to healthy corporate governance practices are indispensable for investor protection.

SEBI's initiative

A study jointly done by the World Bank, rating firm CRISIL and industry chamber FICCI pointed out that shareholder activism tends to be limited in India, and all categories of investors tend to be passive, as far as influencing good corporate governance is concerned. The study had identified weak regulation as a particular concern, given the increased openness and integration of the Indian equity market. Also, the Securities and Exchange Board of India (SEBI) recently expressed its opinion that mutual funds should play an active role in ensuring better corporate governance of listed companies in India.

In furtherance of this objective and as a first step towards plugging the existing lacunas in the system, SEBI released a circular dated 15 March that requires all asset management companies (AMCs) to disclose their general policies and procedures for exercising the voting rights in respect of the shares held by them in investee companies, on the website of the respective AMC and in the annual report distributed to the unit holders from the financial year 2010-11.

Further, SEBI has made it mandatory for AMCs to disclose whether they voted for or against certain matters in the general meetings of investee companies. The items specified in the circular include corporate governance matters such as state of incorporation, merger and other corporate restructuring, and anti-takeover provisions; changes to

capital structure including increases and decreases of capital and preferred stock issuances; stock option plans and other management compensation issues; social and corporate responsibility issues; appointment and removal of directors; and any other issue that may affect the interest of the shareholders in general and interest of the unit holders in particular. The circular goes on to prescribe the manner in which such disclosures are to be made.

Impact of the circular

The mention of social and corporate responsibility issues as a subject which merits mandatory disclosure represents the intention of SEBI to bring greater transparency into the voting patterns of mutual funds. The hope is that such disclosures would push fund houses to take a more active and responsible role as shareholders. This is especially important given that funds quite often possess a sizeable shareholding in companies (in aggregate if not individually).

In light of the requirements specified in the circular, mutual funds will now find themselves in an awkward position if they decide to either abstain from voting or cast proxies without appropriate reasons. The circular is a definite statement of intent from the regulator that there is no scope for institutions to remain as passive spectators in the decisionmaking process.

The circular is a clear indication that SEBI is keen to pave the way for greater shareholder activism and not allow corporate governance in India to be reduced to a mere "box-ticking" exercise.

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