

## **REGULATING PROXY ADVISORY FIRMS IN INDIA**

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### **ABSTRACT**

*The advent of proxy advisors, a decade ago, had barely created any ripples in the Indian corporate waters. Proving otherwise to their critics, proxy advisors have managed to cement their place in the Indian corporate governance agenda through their aggressive push for better governance standards. The growth of proxy advisors denotes a paradigm shift in the approach of making management answerable to minority shareholders. However, given the nature of the task, strife with management and the existence of conflicting interests is inherent. In 2020, SEBI issued circulars directing the development of proxy advisors, who were earlier governed under the broader framework for research analysts. This article analyses the potential impact of the circulars on various stakeholders. The author argues that the circulars have adopted a light-touch approach and has left room for market forces to standardise business practices overtime, instead of being overtly prescriptive. The question whether the safeguards and mechanisms provided under the circulars will be effective in addressing the friction between proxy advisors and management will depend on how the circulars are implemented going forward.*

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## I. INTRODUCTION

The last decade has witnessed proxy advisory firms (PAFs) finding their foothold in the Indian corporate governance agenda.<sup>1</sup> Providing voting recommendations on shareholders' voting items of listed companies is one of their key functions, and institutional investors are their primary clients.<sup>2</sup> Apart from voting advisory, certain PAFs also offer a heterogeneous mix of corporate governance-related consultancy and advisory services in addition to advocating towards better governance standards.<sup>3</sup> The Securities and Exchange Board of India (SEBI) has been proactive in directing development of the PAF industry practices.<sup>4</sup> Recently, SEBI issued circulars on '*Procedural Guidance for Proxy Advisors*' and '*Grievance Resolution between listed entities and proxy advisers*', which are proposed to become applicable from January 1, 2021, apart from certain key

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<sup>1</sup> Nisha Poddar, *Big Deal: India is witnessing a new era of shareholder activism, says Cyril Shroff of Cyril Amarchand Mangaldas*, CNBCTV18 (Nov. 11, 2020, 5.40 P.M.), <https://www.cnbctv18.com/economy/big-deal-india-is-witnessing-a-new-era-of-shareholder-activism-says-cybil-shroff-of-cybil-amarchand-mangaldas-4042621.htm> [hereinafter Nisha Poddar].

<sup>2</sup> Working Group on Issues of Proxy Advisors, *Working Group's Report on Issues Concerning Proxy Advisors*, SECURITIES AND EXCHANGE BOARD OF INDIA, 27 (2019), [https://www.sebi.gov.in/reports/reports/jul-2019/report-of-working-group-on-issues-concerning-proxy-advisors-seeking-public-comments\\_43710.html](https://www.sebi.gov.in/reports/reports/jul-2019/report-of-working-group-on-issues-concerning-proxy-advisors-seeking-public-comments_43710.html) [hereinafter 2019 Report].

<sup>3</sup> Priya Garg, *Ripple, If Not The Waves Effect: Analysing The Way(S) In Which Proxy Advisory Firms Can Affect Corporate Governance In India, In The 'Long Run'*, 5 NAT'L L.U. DELHI STUD. L. J. 111 (2018), 112 (2018), [https://nludelhi.ac.in/download/publication/2018/NLUD%20SLD-Vol.5\(2018\).pdf](https://nludelhi.ac.in/download/publication/2018/NLUD%20SLD-Vol.5(2018).pdf) [hereinafter Priya Garg].

<sup>4</sup> *Consultation Paper on Proposed Regulation of Research Analysts*, SECURITIES AND EXCHANGE BOARD OF INDIA, 5, 7 (2013), [https://www.sebi.gov.in/sebi\\_data/attachdocs/1385713647782.pdf](https://www.sebi.gov.in/sebi_data/attachdocs/1385713647782.pdf).

procedural formalities which are applicable from February 1, 2021.<sup>5</sup> The article will collectively refer to the circular and the modifications issued thereto as ‘Circulars’.<sup>6</sup>

The goal of this article is to analyse the terms of the Circulars and their potential impact on various stakeholders. However, before delving into the analysis of the Circulars in Section IV, to put things into context, Section II of the article will elaborate on the performance of PAFs in India in the past decade; and Section III will trace the evolution of the existing regulatory framework governing PAFs and the factors which lead to SEBI issuing the Circulars.

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<sup>5</sup> *Procedural Guidelines for Proxy Advisors*, (Aug. 3, 2020), SEBI/HO/IMD/DF1/CIR/P/2020/147, [https://www.sebi.gov.in/legal/circulars/aug-2020/procedural-guidelines-for-proxy-advisors\\_47250.html](https://www.sebi.gov.in/legal/circulars/aug-2020/procedural-guidelines-for-proxy-advisors_47250.html) (hereinafter Procedural Guidelines Circular); *Grievance Resolution between listed entities and proxy advisors*, (Aug. 4, 2020), SEBI/HO/CFD/CMD1/CIR/P/2020/119, [https://www.sebi.gov.in/legal/circulars/aug-2020/grievance-resolution-between-listed-entities-and-proxy-advisors\\_47252.html](https://www.sebi.gov.in/legal/circulars/aug-2020/grievance-resolution-between-listed-entities-and-proxy-advisors_47252.html) (hereinafter Grievance Resolution Circular). *Procedural Guidelines for Proxy Advisors’ – Extension of implementation timeline*, (Aug. 27, 2020), SEBI/HO/IMD/DF1/CIR/P/2020/157, [https://www.sebi.gov.in/legal/circulars/aug-2020/procedural-guidelines-for-proxy-advisors-extension-of-implementation-timeline\\_47412.html](https://www.sebi.gov.in/legal/circulars/aug-2020/procedural-guidelines-for-proxy-advisors-extension-of-implementation-timeline_47412.html) (hereinafter Procedural Guidelines Extension Timeline); *Grievance Resolution between listed entities and proxy advisors’ – Extension of timeline for implementation*, (Aug. 27, 2020), SEBI/HO/CFD/CMD1/CIR/P/2020/159, [https://www.sebi.gov.in/legal/circulars/aug-2020/-grievance-resolution-between-listed-entities-and-proxy-advisors-extension-of-timeline-for-implementation\\_47424.html](https://www.sebi.gov.in/legal/circulars/aug-2020/-grievance-resolution-between-listed-entities-and-proxy-advisors-extension-of-timeline-for-implementation_47424.html) (hereinafter Grievance Resolution Extension Timeline). *Procedural Guidelines for Proxy Advisors*, (Dec. 31, 2020), SEBI/HO/IMD/DF1/CIR/P/2020/256, [https://www.sebi.gov.in/legal/circulars/dec-2020/procedural-guidelines-for-proxy-advisors\\_48633.html](https://www.sebi.gov.in/legal/circulars/dec-2020/procedural-guidelines-for-proxy-advisors_48633.html) (hereinafter Modification Circular).

<sup>6</sup> Procedural Guidelines Circular, Grievance Resolution Circular, Procedural Guidelines Extension Timeline, Grievance Resolution Extension Timeline and Modification Circular are collectively referred to as Circulars.

For the purpose of this article, the author is assuming that encouraging growth of PAFs as corporate governance intermediaries will lead to implementing better corporate governance standards.<sup>7</sup> Further, the author is also assuming that increasing institutional ownership and their role in the burgeoning Indian capital markets as active participants of corporate decision-making is encouraged.<sup>8</sup> Given that there is sufficient literature<sup>9</sup> justifying the basis for these assumptions, the article will not be addressing them, except in relation to evaluating PAF performance in Section II of this article.

## II. SETTING THE CONTEXT: PERFORMANCE REPORT 2010-2020

The first domestic PAF was set up in 2010.<sup>10</sup> Currently, there are three home-grown<sup>11</sup> and several global PAFs (out of which two

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<sup>7</sup> See Umakanth Varottil, *The Advent of Shareholder Activism in India*, 602 (2012), 1(6) J. OF GOVERNANCE; Michael Cappucci, *The proxy war against proxy advisors*, 16(3) N.Y.U. J. L. & BUS. 579, 580-632 (2020) [hereinafter Cappucci]; Cyril Shroff, *Corporate Governance & Shareholder Activism*, INDIA CORPORATE LAW (Apr. 16, 2016), <https://corporate.cyrilamarchandblogs.com/2016/04/corporate-governance-shareholder-activism/#more-1867>[hereinafter Cyril Shroff].

<sup>8</sup> See Umakanth Varottil, *Shareholder Stewardship in India: The Desiderata*, NUS LAW WORKING PAPER SERIES 2020/005, (2020),<http://law.nus.edu.sg/wps/> [hereinafter Umakanth Varottil]; P. Krishna Prasanna & Anish S Menon, *Corporate Governance and stock market liquidity in India*, I NTL J. BEHAVIOURAL ACCNT'G. & FIN., (2011), <https://ssrn.com/abstract=1735808>; Manjit Kaur Sidhu, *Corporate Governance and Stock Market Liquidity*, 5(3) J. Com. & ACCNT'G R., (2016).

<sup>9</sup> *Id.*

<sup>10</sup> See S. Subramanian, *Proxy Advisory Industry in India*, 13(2) CORPORATE OWNERSHIP & CONTROL, 371-378 (2016), [https://www.virtusinterpress.org/IMG/pdf/10-22495\\_cocv13i2cLp5.pdf](https://www.virtusinterpress.org/IMG/pdf/10-22495_cocv13i2cLp5.pdf);

have significant presence in India and one of them is registered with SEBI)<sup>12</sup>, which are active in India. While offering voting advisory is a common thread, the business model followed and the service offered by them are not homogenous.<sup>13</sup>

After the initial skepticism,<sup>14</sup> the stakeholders have gradually started acknowledging the influence of PAFs.<sup>15</sup> Over the span of the last decade, the sphere of coverage of PAFs has expanded.<sup>16</sup> Further, given the nature of their engagement, PAFs often find themselves in a unique position where their recommendations have the potential to influence the dispersed institutional investors' vote. Additionally, earlier, given the minority stake held by most institutional investors, they preferred to follow the equivalent to the 'Wall Street Rule',<sup>17</sup> where they either voted with the management or abstained from voting.<sup>18</sup> However, as has been demonstrated in

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<sup>11</sup> See INGVERN, <http://www.ingovern.com/> (Nov. 11, 2020); INSTITUTIONAL INVESTOR ADVISORY SERVICES (IIAS), <https://www.iiasadvisory.com/> (Nov. 11, 2020); and STAKEHOLDERS EMPOWERMENT SERVICES (SES), <https://www.sesgovernance.com> (Nov. 11, 2020).

<sup>12</sup> 2019 Report, *supra* note 2.

<sup>13</sup> 2019 Report, *supra* note 2.

<sup>14</sup> N. Sundaresha Subramanian & Sudipto Dey, *Proxy firms lead change in governance framework*, BUSINESS STANDARD (Ju. 9, 2015), [https://www.business-standard.com/article/markets/proxy-firms-lead-change-in-governance-framework-115070900757\\_1.html](https://www.business-standard.com/article/markets/proxy-firms-lead-change-in-governance-framework-115070900757_1.html) [hereinafter N. Sundaresha Subramanian & Sudipto Dey].

<sup>15</sup> Nisha Poddar, *supra* note 1.

<sup>16</sup> For example, IiAS claims to have covered more than 800 companies and issued more than 47,000 recommendations, <https://www.iiasadvisory.com/> (Nov. 11, 2020).

<sup>17</sup> Cappucci, *supra* note 7.

<sup>18</sup> Institutional Investor Advisory Services, *Institutional Investors: Growing heft*, INSTITUTIONAL EYE, (Feb 17, 2020) [https://docs.wixstatic.com/ugd/91c61f\\_374047565b594007a83e9dae9d832aee.pdf](https://docs.wixstatic.com/ugd/91c61f_374047565b594007a83e9dae9d832aee.pdf).

recent literature,<sup>19</sup> India is witnessing a gradual shift in institutional investors' involvement: i.e. from opting from a 'Wall Street Walk'<sup>20</sup> approach to actively participating in decision making.<sup>21</sup> The enhanced role of institutional investors can be argued to have contributed to the relevance of PAFs' recommendations.

Without delving into granular details, some of the factors which have led to this shift towards institutional investors playing a greater role include, *inter alia*, the following:

- (i) Increase of institutional ownership from about 22% to about 35% in the last 12 years;<sup>22</sup>
- (ii) Stewardship obligation being imposed on fund managers  
(SEBI introduced a consolidated stewardship code in India effective from 2020,<sup>23</sup> however Insurance Regulatory and Development

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<sup>19</sup> Umakanth Varottil, *supra* note 8.

<sup>20</sup> Institutional Investor Advisory Services, *India's progress on the Corporate Governance agenda: An overview*, INSTITUTIONAL EYE, (Nov. 11, 2020), [https://mcusercontent.com/ad513546cf36ede008c1097c7/files/4c2cdc3d-d866-4a5b-ba52-86e919f5dc84/ICGN\\_IndiaTalkingPoints\\_HetalDalal\\_11Nov2020.pdf](https://mcusercontent.com/ad513546cf36ede008c1097c7/files/4c2cdc3d-d866-4a5b-ba52-86e919f5dc84/ICGN_IndiaTalkingPoints_HetalDalal_11Nov2020.pdf) [hereinafter Institutional Investor Advisory Services].

<sup>21</sup> Cyril Shroff & Amita Katragadda, *India Corporate Governance Laws and Regulations 2020*, ICLG (Nov. 11, 2020, 5.45 P.M.), <https://iclg.com/practice-areas/corporate-governance-laws-and-regulations/india>.

<sup>22</sup> Institutional Investor Advisory Services, *supra* note 20.

<sup>23</sup> *Stewardship Code for all Mutual Funds and all categories of AIFs, in relation to their investment in listed equities*, (Dec. 24, 2019), CIR/CFD/CMD1/168/2019, [https://www.sebi.gov.in/legal/circulars/dec-2019/stewardship-code-for-all-mutual-funds-and-all-categories-of-aifs-in-relation-to-their-investment-in-listed-equities\\_45451.html](https://www.sebi.gov.in/legal/circulars/dec-2019/stewardship-code-for-all-mutual-funds-and-all-categories-of-aifs-in-relation-to-their-investment-in-listed-equities_45451.html); *Extension of deadline for implementation of the circular on Stewardship Code for all Mutual Funds and all categories of AIFs due to the CoVID-19 pandemic*, (Mar. 30, 2020), SEBI/HO/CFD/CMD1/CIR/P/2020/55, <https://www.sebi.gov.in/legal/circulars/mar-2020/extension-of-deadline-for->

*Authority of India,*<sup>24</sup> *Pension Fund Regulatory and Development Authority*<sup>25</sup> and *SEBI (for mutual funds)*<sup>26</sup> had issued guidelines in line with stewardship and fiduciary obligations in 2017, 2018 and 2010, respectively);

- (iii) Ease of access to corporate information and voting facilities;<sup>27</sup> and
- (iv) A requirement of majority of minority approval for certain items which have notable impact on corporate governance.<sup>28</sup>

These factors noted above, among other things, can be argued to have cumulatively led to institutional investors, and consequently their advisors, PAFs, acquiring a significant role in Indian corporate decision-making.

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implementation-of-the-circular-on-stewardship-code-for-all-mutual-funds-and-all-categories-of-aifs-due-to-the-covid-19-pandemic\_46451.html.

<sup>24</sup> See *Guidelines on Stewardship Code for Insurers in India*, (Mar. 22, 2017), Ref. No: IRDA/F&A/GDL/CMP/059/03/2017,

[https://www.irdai.gov.in/ADMINCMS/cms/whatsNew\\_Layout.aspx?page=PageNo3096&flag=1](https://www.irdai.gov.in/ADMINCMS/cms/whatsNew_Layout.aspx?page=PageNo3096&flag=1); *Revised Guidelines on Stewardship Code for Insurers in India*, (Feb. 7, 2020), Ref. No:IRDAI/F&A/GDL/CPM/045/02/2020,[https://www.irdai.gov.in/ADMINCMS/cms/whatsNew\\_Layout.aspx?page=PageNo4045&flag=1](https://www.irdai.gov.in/ADMINCMS/cms/whatsNew_Layout.aspx?page=PageNo4045&flag=1).

<sup>25</sup> See *Common Stewardship Code*, (May 4, 2018), PFRDA/2018/01/PF/01, <https://www.pfrda.org.in/writereaddata/links/circular-%20common%20stewardship%20code%2004-05-186ec9a3b4-566b-4881-b879-c5bf0b9e448a.pdf>.

<sup>26</sup> See *Circular for Mutual Funds*, SEBI/IMD/CIR No 18/198647/2010 (15 March 2010), [https://www.sebi.gov.in/legal/circulars/mar-2010/circular-for-mutual-funds\\_2019.html](https://www.sebi.gov.in/legal/circulars/mar-2010/circular-for-mutual-funds_2019.html).

<sup>27</sup> Priya Garg, *supra* note 3.

<sup>28</sup> Sachin P. Mampatta, *Small Guys Can Punch above Their Weight*, BUSINESS STANDARD (Jul. 29, 2014), [http://www.business-standard.com/article/markets/small-guys-can-punch-above-theirweight-114082901000\\_1.html](http://www.business-standard.com/article/markets/small-guys-can-punch-above-theirweight-114082901000_1.html).

Given the nature of the role played by PAFs, their success stories are not evident.<sup>29</sup> One probable rationale could be that given the stewardship obligation of fund managers, glorifying or advertising their excessive reliance on PAFs may raise allegations of 'lazy stewardship'.<sup>30</sup> Therefore, while ample evidences of institutional investors defeating resolutions are available in the public domain,<sup>31</sup> empirical evidence<sup>32</sup> of instances where such a decision was influenced by PAF recommendation is not easily available in India. This has made it difficult to analyse the areas of governance where PAFs hold a significant say.

Nevertheless, on the basis of some of the notable reported instances, it can be deduced, although at the risks of generalising and confusing coincidence with co-relation, that PAFs may have impacted the following areas of governance in India in the last decade:

- (i) Related party transactions (including payment of royalty)

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<sup>29</sup> 2019 Report, *supra* note 2.

<sup>30</sup> *Outsourcing corporate governance – Are proxy advisors measuring up to expectations?*, NSE-ECGI ROUNDTABLE ON LONG TERM IMPACT OF INSTITUTIONAL OWNERSHIP ON GOVERNANCE AND SUSTAINABLE INVESTMENT (Nov. 13, 2017), [https://archives.nseindia.com/products/resources/download/NSE\\_ECGL\\_Mumbai\\_roundtable\\_report\\_2017.pdf](https://archives.nseindia.com/products/resources/download/NSE_ECGL_Mumbai_roundtable_report_2017.pdf).

<sup>31</sup> Pawan Burugula, Rajesh Mascarenhas & Prashant Mahesh, *Vocal FII's give company managements a tough time*, THE ECONOMIC TIMES (Aug. 26, 2020), <https://economictimes.indiatimes.com/markets/stocks/news/vocal-fis-stall-appointment-of-underperforming-directors/articleshow/77753995.cms>.

<sup>32</sup> 2019 Report, *supra* note 2.



*Examples: (i) Nestle India Limited's initial proposal to seek approval for payment of royalty in perpetuity was revised to a fixed time frame after PAFs and investors expressed reservations (2019);<sup>33</sup>(ii) Raymond Limited's proposal in relation to sale of immovable property to a related party was defeated (2017);<sup>34</sup> and (iii) United Spirits Limited – Diagio' proposal to ratify related party transactions with entities associated with then Chairman Vijay Malhya was questioned (2014).<sup>35</sup>*

(ii) Director (including independent director) appointments and re-appointments

*Examples: (i) Lakshmi Vilas Bank (2020);<sup>36</sup> (ii) HDFC Limited (2018);<sup>37</sup> (iii) Infosys Limited (2017);<sup>38</sup> (iv) Raymond Limited (2017);<sup>39</sup> and (v) IDFC Limited (2017).<sup>40</sup>*

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<sup>33</sup> Institutional Investor Advisory Services, *Royalty payments: Too early to take your eyes off* INSTITUTIONAL EYE, (Feb. 20, 2020), [https://docs.wixstatic.com/ugd/6e1ce5\\_1feca2706ded4c64b8095ddc19834143.pdf](https://docs.wixstatic.com/ugd/6e1ce5_1feca2706ded4c64b8095ddc19834143.pdf).

<sup>34</sup> *LIC reduces stake in Raymond by 2.01%*, BLOOMBERG QUINT (Sept. 6, 2017), <https://www.bloomberqunt.com/markets/2017/09/06/lic-reduces-stake-in-raymond-by-201>.

<sup>35</sup> N. Sundaresha Subramanian & Jayshree P. Upadhyay, *United Spirits' private deals come into question*, BUSINESS STANDARD (Nov. 3, 2014), [https://www.business-standard.com/article/companies/united-spirits-private-deals-come-into-question-114112200823\\_1.html](https://www.business-standard.com/article/companies/united-spirits-private-deals-come-into-question-114112200823_1.html).

<sup>36</sup> Atmadip Ray, *Lakshmi Vilas Bank directors lacked accountability: Advisory firm*, THE ECONOMIC TIMES (Sept. 27, 2020), <https://economictimes.indiatimes.com/markets/stocks/news/lakshmi-vilas-bank-directors-lacked-accountability-advisory-firm/articleshow/78345414.cms>.

<sup>37</sup> *Foreign proxy advisory firms need domestic regulation: Uday Kotak*, THE ECONOMIC TIMES (Aug. 7, 2018), <https://economictimes.indiatimes.com/news/company/corporate-trends/foreign-proxy-advisory-firms-need-domestic-regulation-uday-kotak/articleshow/65300546.cms>.

## (iii) Executive remuneration

*Examples: (i) Apollo Tyres Limited (2018),<sup>41</sup> (ii) ITC Limited (2017),<sup>42</sup> (iii) Tata Motors Limited (2014-2015),<sup>43</sup> and (iv) HCC Limited (2014-2015).<sup>44</sup>*

## (iv) Transactions impacting long term interest of the company/minority shareholder's interest

*Examples: (i) Payment of non-compete fees to Max Financial in relation to the HDFC Life and Max Financial merger (2016),<sup>45</sup> (ii) Crompton Greaves Limited restructuring (2014-2015),<sup>46</sup> (iii) Maruti-Suzuki's proposal for procuring parts from related party, instead of captive manufacture*

<sup>38</sup> Anand Adhikari, *The lone wolf*, BUSINESS TODAY (Feb. 25, 2018), <https://www.businesstoday.in/magazine/the-hub/the-lone-wolf/story/269874.html> [hereinafter Anand Adhikari].

<sup>39</sup> *Id.*

<sup>40</sup> *Id.*

<sup>41</sup> *Victory for minority shareholders in Apollo Tyres: Kanwars to take a 30% salary cut*, FINANCIAL EXPRESS (Nov. 14, 2018), <https://www.financialexpress.com/industry/victory-for-minority-shareholders-in-apollo-tyres-kanwars-to-take-a-30-cut-in-salary/1381109/>.

<sup>42</sup> Anand Adhikari, *supra* note 38.

<sup>43</sup> N. Sundaresha Subramanian & Sudipto Dey, *supra* note 14.

<sup>44</sup> *HCC recovers chairman's 'excess' salary*, BUSINESS STANDARD (May 1, 2015), [https://www.business-standard.com/article/companies/hcc-recovers-chairman-s-excess-salary-115043000791\\_1.html](https://www.business-standard.com/article/companies/hcc-recovers-chairman-s-excess-salary-115043000791_1.html).

<sup>45</sup> Anand Adhikari, *supra* note 38.

<sup>46</sup> Rajesh Mascarenhas, *Minority shareholders increasingly having a say in key decisions of companies*, THE ECONOMIC TIMES (Feb. 26, 2015), <https://economictimes.indiatimes.com/markets/stocks/news/minority-shareholders-increasingly-having-a-say-in-key-decisions-of-companies/articleshow/46377944.cms?from=mdr>.

(2014-2015),<sup>47</sup> (iv) *Azko-Nobel's restructuring (2012)*,<sup>48</sup> and (v) *Sesa-Sterlite restructuring (2012)*.<sup>49</sup>

It is pertinent to note that PAFs have not been spared the ire of Indian management and have faced severe backlash, often from the impugned management. For example, ITC Limited filed a Rs. 1000 crore defamation suit against Institutional Investor Advisory Services for statements made against the company and its management in 2017.<sup>50</sup> In 2018, Mr. Uday Kotak, a veteran banker and Chairman of the Committee of Corporate Governance, SEBI,<sup>51</sup> highlighted the need for regulation of foreign PAFs in India, after such PAFs, applying standards more stringent than applicable laws, voted against the appointment of another veteran banker Mr. Deepak Parekh on the board of HDFC Ltd.<sup>52</sup>

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<sup>47</sup> Cyril Shroff, *supra* note 7.

<sup>48</sup> N. Sundaresha Subramanian & Sudipto Dey, *supra* note 14.

<sup>49</sup> *Shareholder activism in India*, INGOVERN, <http://www.ingovern.com/2015/02/shareholder-activism-in-india/>.

<sup>50</sup> ITC Ltd. v. Institutional Investor Advisory Services, High Court of Calcutta, GA No.4075 of 2017; *See also*, Sundaresh Subramanian, *Should SEBI Save Analysts From Their Subjects?*, BUSINESS STANDARD (Sept. 12, 2017), <https://www.pressreader.com/india/business-standard/20170912/281981787749511>.

<sup>51</sup> *Report of the Committee on Corporate Governance* (Oct. 5, 2017), [https://www.sebi.gov.in/reports/reports/oct-2017/report-of-the-committee-on-corporate-governance\\_36177.html](https://www.sebi.gov.in/reports/reports/oct-2017/report-of-the-committee-on-corporate-governance_36177.html).

<sup>52</sup> Sajeet Manghat, *Uday Kotak Wants India To Regulate International Proxy Advisers*, BLOOMBERG QUINT (Aug. 6, 2018), <https://www.bloombergquint.com/business/uday-kotak-wants-india-to-regulate-international-proxy-advisers> [hereinafter Sajeet Manghat].

### III. SETTING THE CONTEXT: EVOLUTION OF REGULATIONS GOVERNING PAFS IN INDIA

PAFs are primarily regulated by SEBI under the SEBI (Research Analysts) Regulations, 2014 (RA Regulations).<sup>53</sup> Their conduct may also bring them under the purview of other securities market regulations like regulations against insider trading, prevention of fraudulent and unfair trade practices etc. For the purpose of this article, the author will only focus on the evolution of the RA Regulations and the subsequent Circulars issued thereunder.

In the backdrop of the then persisting global financial crisis of 2008, role of research analysts, particularly sell-side analysts and credit rating agencies, was brought to scrutiny.<sup>54</sup> With the objective of setting international standards for financial market intermediaries, an action plan to implement the ‘Common Principles for Reform of Financial Markets’ was proposed at the Washington G20 Summit in

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<sup>53</sup> Securities and Exchange Board of India (Research Analysts) Regulations, 2014, [https://www.sebi.gov.in/sebi\\_data/commndocs/RESEARCHANALYSTS-regulations\\_p.pdf](https://www.sebi.gov.in/sebi_data/commndocs/RESEARCHANALYSTS-regulations_p.pdf) (Nov. 11, 2020) (hereinafter RA Regulations); *See also, Frequently Asked Questions – SEBI (Research Analysts) Regulations, 2014*, [https://www.sebi.gov.in/sebi\\_data/faqfiles/jan-2017/1485860192812.pdf](https://www.sebi.gov.in/sebi_data/faqfiles/jan-2017/1485860192812.pdf) (Nov. 11, 2020).

<sup>54</sup> *Plan of Actions for Compliance To Eight New IOSCO Objectives and Principles of Securities Regulation*, SEBI Board Meeting Agenda (Jul. 28, 2011), [https://www.sebi.gov.in/sebi\\_data/meetingfiles/1313055313828-a.pdf](https://www.sebi.gov.in/sebi_data/meetingfiles/1313055313828-a.pdf) (hereinafter IOSCO POA); *See also, SEBI Board Meeting Decision* (Jul. 28, 2011), [https://www.sebi.gov.in/sebi\\_data/meetingfiles/1323341185009-d.pdf](https://www.sebi.gov.in/sebi_data/meetingfiles/1323341185009-d.pdf).

2008,<sup>55</sup> which called for a review of the functioning of such intermediaries. International Organization of Securities Commissions (IOSCO), in collaboration with Basel Committee on Banking Supervision and the International Association of Insurance Supervisors, was tasked with the said responsibility and their recommendations were reported in ‘Differentiated Nature and Scope of Financial Regulation’.<sup>56</sup> This report, among other things, recommended that the core principles of the global securities market, codified under the IOSCO Objectives and Principles of Securities Regulation (IOSCO Principles), be reviewed to ensure addressal of systemic risks.<sup>57</sup> Accordingly, one of the key agendas was the scrutiny of the role of entities that offer investors analytical or evaluative services, and the strengthening of a mechanism to address the inherent conflict of interest.<sup>58</sup> It is pertinent to note that PAFs were not specifically a subject matter of the discussions; rather the focus was on the conduct of sell-side analysts, whose risk of being conflicted was concluded to be significant. The revised IOSCO Principles was approved at the IOSCO 2010 Annual

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<sup>55</sup> *Declaration Summit on Financial Markets and The World Economy*, G-20 2 (Nov. 15, 2008), <https://g20.org/en/g20/Documents/2008-Washington-Declaration%20of%20the%20Summit%20on%20Financial%20Markets%20and%20the%20World%20Economy.pdf>.

<sup>56</sup> International Organization of Securities Commissions, Basel Committee on Banking Supervision & International Association of Insurance Supervisors, *Review of the Differentiated Nature and Scope of Financial Regulation Key Issues and Recommendations* (Jan. 2010), [https://www.iosco.org/library/pubdocs/pdf/IOSCO\\_PD315.pdf](https://www.iosco.org/library/pubdocs/pdf/IOSCO_PD315.pdf) [hereinafter 2010 Report]; IOSCO POA, *supra* note 54..

<sup>57</sup> 2010 Report, *supra* note 56.

<sup>58</sup> IOSCO POA, *supra* note 54.

Conference.<sup>59</sup> Principle 23 which stated that “*other entities that offer investors analytical or evaluative services should be subject to oversight and regulation appropriate to the impact their activities have on the market or the degree to which the regulatory system relies on them*”<sup>60</sup> was introduced, which thereafter became the genesis of regulations applicable to research analysts, including PAFs.

SEBI undertook a self-assessment exercise to ensure compliance with the new IOSCO Principles.<sup>61</sup> On the basis of such exercise, it concluded that there was a regulatory gap when it came to regulation of research analysts and the same should be put in place.<sup>62</sup> The same conclusion was arrived at the November 5, 2012 meeting of the International Advisory Board of SEBI as well.<sup>63</sup> Again, the primary concern at this stage continued to be issues in relation to conflict of interest of analysts like sell-side analysts; and PAFs were not a matter of concern. This is likely because in 2011-2012, with domestic PAFs having set up shop only in 2010, considering regulating PAFs would have been premature.

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<sup>59</sup> Media Release OICU-IOSCO, *Global securities regulators adopt new principles and increase focus on systemic risk*, IOSCO/MR/10/2010 (Jun. 10, 2020), <https://www.iosco.org/news/pdf/IOSCONEWS188.pdf>.

<sup>60</sup> OICU-IOSCO, *Objective and Principles of Securities Regulations*, <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD561.pdf> (Nov. 11, 2020).

<sup>61</sup> IOSCO POA, *supra* note 54.

<sup>62</sup> IOSCO POA, *supra* note 54.

<sup>63</sup> Press Release, International Advisory Board of SEBI PR No.: 93/201293/2012 (Nov. 5, 2012), [https://www.sebi.gov.in/media/press-releases/nov-2012/international-advisory-board-of-sebi-meets-at-mumbai\\_23712.html](https://www.sebi.gov.in/media/press-releases/nov-2012/international-advisory-board-of-sebi-meets-at-mumbai_23712.html).

SEBI issued the ‘Consultation Paper on Proposed Regulation of Research Analysts’ along with draft RA Regulations for public comments in November 2013.<sup>64</sup> PAFs, as a category of entity publishing research reports, was recognised categorically and was sought to be brought under the umbrella of the RA Regulations. This approach of SEBI was a deviation from the ‘comply or explain’ model being followed by most foreign securities market regulators at that time.<sup>65</sup> It was, however, proposed that PAFs would not be required to be registered with SEBI, unless they made their recommendations through public media.<sup>66</sup>

Subsequently, the RA Regulations came into force on September 1, 2014.<sup>67</sup> It defined PAFs as “*any person who provide advice, through any means, to institutional investor or shareholder of a company, in relation to exercise of their rights in the company including recommendations on public offer or voting recommendation on agenda items*”<sup>68</sup> and became the primary regulation for PAFs in India. Deviating from its initial proposal, SEBI put in place a mechanism for registration of PAFs. This requirement of mandatory registration has been argued by some, to

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<sup>64</sup> *Consultation Paper on Proposed Regulation of Research Analysts*, SECURITIES AND EXCHANGE BOARD OF INDIA (2013), [https://www.sebi.gov.in/sebi\\_data/attachdocs/1385713647782.pdf](https://www.sebi.gov.in/sebi_data/attachdocs/1385713647782.pdf) (hereinafter RA Consultation Paper); *See also*, Press Release, PR No. 114/2013 (Nov. 29, 2013), [https://www.sebi.gov.in/sebi\\_data/docfiles/26869\\_t.html](https://www.sebi.gov.in/sebi_data/docfiles/26869_t.html).

<sup>65</sup> RA Consultation Paper, *Id.*

<sup>66</sup> RA Consultation Paper, *Id.*

<sup>67</sup> RA Regulations, *supra* note 53.

<sup>68</sup> RA Regulations, Reg. 2 (p), *supra* note 53.

be a stamp of their legitimacy, especially in the Indian market where they are being pitted against Indian Goliathic listed company managements.<sup>69</sup> As per the RA Regulations, PAFs are obligated to follow the same standards as applicable to other research analysts (the provisions having been made applicable *mutatis mutandis* to PAFs), in addition to certain incremental diktats.<sup>70</sup> These include regulations relating to quality control (for example: standard of skill of analysts;<sup>71</sup> disclosure of research methodology;<sup>72</sup> record keeping of recommendations<sup>73</sup> etc.) and capital adequacy requirements.<sup>74</sup>

This article will not delve into a critique of the RA Regulations as the same has been discussed exhaustively in existing literature,<sup>75</sup> other than as may be necessary to analyse the Circulars. Nevertheless, it is pertinent to bear in mind that treatment of PAFs at par with other research analysts leads to a situation where the regulations are not tailored to suit the business requirements of PAFs. This one-size-fits-all approach leads to the stakeholders involved facing several issues.<sup>76</sup> Such issues drew public<sup>77</sup> as well as

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<sup>69</sup> Nisha Poddar, *supra* note 1.

<sup>70</sup> RA Regulations, Regs. 23 & 24, *supra* note 53.

<sup>71</sup> RA Regulations, Reg 23(1), *supra* note 53.

<sup>72</sup> RA Regulations, Reg 23(2), *supra* note 53.

<sup>73</sup> RA Regulations, Reg 23(3), *supra* note 53.

<sup>74</sup> RA Regulations, Reg 23(1), *supra* note 53.

<sup>75</sup> Priya Garg, *supra* note 3.

<sup>76</sup> 2019 Report, *supra* note 2.

<sup>77</sup> Sajeet Manghat, *supra* note 52. See also, Souvik Ganguly & Aman Bagaria, *Why proxy advisors will assume greater significance in coming years*, VCCIRCLE (Oct. 19, 2020),



SEBI's attention since the PAFs started assuming a greater role. To address these issues, SEBI set up a working committee under the helm of Mr. Sandeep Parekh, which issued its report on issues concerning PAFs in 2019 (2019 Report),<sup>78</sup> and thereafter to implement such recommendations from the 2019 Report, the Circulars<sup>79</sup> were issued. Coincidentally, these developments are in tandem with comparable regulatory efforts of Securities Exchange Commission (SEC), even though, the causal factors may not be similar.<sup>80</sup>

#### **IV. ANALYSIS: POTENTIAL IMPACT OF THE CIRCULARS ON RELEVANT STAKEHOLDERS**

The 2019 Report analysed the business model of PAFs and addressed the issues being raised by PAFs and stakeholders i.e. listed companies and clients of PAFs, including institutional investors.<sup>81</sup> While highlighting the nascency of PAFs in India, the report stressed on not imposing such restrictions, which will either curtail existing competition or deter new entrants to the proxy advisory

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<https://www.vccircle.com/why-proxy-advisors-will-assume-greater-significance-in-coming-years>.

<sup>78</sup> 2019 Report, *supra* note 2.

<sup>79</sup> *Supra* note 5.

<sup>80</sup> Cappucci, *supra* note 7; U.S. Securities and Exchange Commission Press Release, *SEC Adopts Rule Amendments to Provide Investors Using Proxy Voting Advice More Transparent, Accurate and Complete Information* (Jul. 2020), <https://www.sec.gov/news/press-release/2020-161>.

<sup>81</sup> 2019 Report, *supra* note 2.

industry.<sup>82</sup> While the 2019 Report prescribed business practices which will address conflicting concerns (particularly, in relation to quality of disclosures), the sole legal amendment it recommended to SEBI was inclusion of the provision for a grievance redressal mechanism.<sup>83</sup> In light of the 2019 Report, SEBI issued the Circulars.<sup>84</sup> The impact of the Circulars on the relevant stakeholders is discussed below:

## **A. IMPACT ON PAFs<sup>85</sup>**

### **1. Applicability**

The Circulars are unclear regarding their applicability to foreign PAFs. Currently, apart from the requirement of entering into an agreement with a SEBI registered research analyst,<sup>86</sup> a foreign PAF is not required to be registered under the RA Regulations. Given that the Circulars are issued under the RA Regulations, it can be argued that these Circulars will not be binding on foreign PAFs. This approach is consistent with the 2019 Report, which recommended that SEBI should put in place a non-binding code of conduct for foreign PAFs, instead of subjecting them to

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<sup>82</sup> 2019 Report, *supra* note 2.

<sup>83</sup> 2019 Report, *supra* note 2.

<sup>84</sup> *Supra* note 5.

<sup>85</sup> See also Umakanth Varottil, *SEBI Tightens Reins over the Proxy Advisory Industry*, INDIA CORP LAW (Aug. 4, 2020), <https://indiakorplaw.in/2020/08/sebi-tightens-reins-over-the-proxy-advisory-industry.html>.

<sup>86</sup> RA Regulations, Reg 4, *supra* note 53.

Indian regulations, thereby encouraging their participation in domestic market.<sup>87</sup>

## **2. Conflict of interest**

As per the Circulars, a disclosure in relation to conflict of interest and the safeguards for mitigating against them is required to be made on every advice shared by PAFs.<sup>88</sup> In case of any ‘potential conflict of interest’, PAFs are required to follow the same standard.<sup>89</sup> Further, in case they are engaged in other business activities, including consultancy services, they are required to put in place procedures to disclose, manage and mitigate any potential resultant conflict of interest.<sup>90</sup>

While this obligation is in line with the purpose behind implementation of the RA Regulations (as discussed in Section III above), this gives limited guidance regarding how it should be implemented. For example, the 2019 Report had provided the following recommendations/clarifications on this issue, which the Circulars have not included: (a) creation of ‘Chinese Walls’ or housing business in separate units, if PAFs offered consultancy or advisory services; (b) generic disclosure/disclaimer not being enough to satisfy the standards of avoidance of conflict; (c) making

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<sup>87</sup> 2019 Report, *supra* note 2.

<sup>88</sup> Para 1(g), Procedural Guidelines Circular, *supra* note 5.

<sup>89</sup> Para 1(g), Procedural Guidelines Circular, *supra* note 5.

<sup>90</sup> Para 1(h), Procedural Guidelines Circular, *supra* note 5.

disclosures regarding the business model of PAFs (including: types of services provided, revenue breakup from various services, categories of clients served and any specific prohibition on services provided); (d) board of PAFs being independent of its shareholders in cases where shareholders are conflicted and disclosure of substantial shareholding or inter-locked boards; and (e) limiting disclosures regarding affiliate business only when such businesses exceeded a prescribed percentage of revenue etc.<sup>91</sup>

Further, what amounts to ‘potential conflict’ is unclear and is left to the subjective determination of the PAFs. Situations may arise where PAFs may not be aware of such potential conflict at the time of making such disclosure.

While it is open for debate whether 2019 Report was overly prescriptive in this regard, some guidance from SEBI would have been helpful. Especially, since the provisions of the RA Regulations and the applicable code of conduct<sup>92</sup> already have provisions obligating PAFs to address such conflict of interest which impacts their impartiality and make disclosures regarding the same. Further, research analysts are also directed to have adequate mechanisms to ensure independence of their research activities from their other

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<sup>91</sup> 2019 Report, *supra* note 2.

<sup>92</sup> RA Regulations, Reg. 24(2) read with Code of Conduct, *supra* note 53.

business activities.<sup>93</sup> Therefore, the incremental clarification issued under the Circulars fails to clear the confusion regarding what might be acceptable as an adequate disclosure, particularly in relation to ‘potential conflicts’.

### 3. Standardisation of practice

Following the 2019 Report and codifying the existing market practise, the Circulars propose that PAFs should put in place a voting recommendation policy which has to be followed while recommending.<sup>94</sup> The said policy should be reviewed and updated annually.<sup>95</sup> The policy should also clarify scenarios where PAFs will not issue recommendations.<sup>96</sup> These practices are directed towards creating transparency and accountability. The Circulars are silent whether it will be possible to deviate from the policy to allow for flexibility and addresses concerns of PAFs providing one-size-fits-all recommendations.

PAFs are also required to disclose their research methodology as well as the manner in which they came to its conclusion.<sup>97</sup> There is no clarity provided regarding the quality of disclosures in relation

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<sup>93</sup> RA Regulations, Reg. 15, *supra* note 53.

<sup>94</sup> Para 1(a), Procedural Guidelines Circular, *supra* note 5.

<sup>95</sup> Para 1(a), Procedural Guidelines Circular, *supra* note 5.

<sup>96</sup> Para 1(a), Procedural Guidelines Circular, *supra* note 5.

<sup>97</sup> Para 1(b), Procedural Guidelines Circular, *supra* note 5.

to what amounts to research methodology.<sup>98</sup> For example, the 2019 Report had clarified that disclosure of methodology could involve the following: “(a) the general approach that leads to the generation of research; (b) the information sources used; (c) the extent to which local conditions and customs are taken into account; (d) the extent to which custom or house voting policies or guidelines may be applied; and, (e) the systems and controls deployed to reasonably ensure the reliability of the use of information in the research process, and the limitations thereof”.<sup>99</sup> Additionally, as per the 2019 Report, institutional investors should not be involved in preparation of the recommendations to ensure impartiality.<sup>100</sup> Given the lack of clarity, PAFs have the discretion to determine the extent of disclosure, particularly in cases where such disclosure may compromise their edge over their competitors. Further, one can argue that the requirement of including such additional information will make PAF’s task cumbersome, especially since they function within tight deadlines<sup>101</sup>.

Additionally, PAFs are also required to disclose in their recommendations the difference between the legal requirement vis-

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<sup>98</sup> See Daksh Aggarwal, *Beware Proxy Advisers! The Big Brother is Watching: Key Issues with SEBI’s Puzzling Guidelines for Proxy Advisers*, THE CONTEMPORARY LAW FORUM (Oct.14, 2020), <https://tclf.in/2020/10/14/beware-proxy-advisers-the-big-brother-is-watching-key-issues-with-sebis-puzzling-guidelines-for-proxy-advisers>.

<sup>99</sup> 2019 Report, *supra* note 2.

<sup>100</sup> 2019 Report, *supra* note 2.

<sup>101</sup> The timelines for holding shareholding meetings are prescribed by the Ministry of Corporate Affairs, Companies Act, 2013 read with the applicable rules framed thereunder.

a-vis any higher standard which is being applied, as well as the rationale behind it.<sup>102</sup> This requirement will be useful in providing clarity to foreign investors who are not familiar with Indian legal standards. However, it is unclear if this obligation will be satisfied if such deviations are included in the voting guidelines instead of the reports for the sake of reducing the workload of PAFs.

#### **4. Interaction with listed companies**

In relation to PAF's interaction with listed companies, SEBI has prescribed the following methodology:<sup>103</sup>

- (a) Simultaneous sharing of report with listed company and clients;
- (b) Adoption of a policy prescribing the manner in which any information is shared with the listed company;
- (c) Comments/clarifications received from listed company, within the timeline adopted by PAFs at its discretion, to be disclosed as addendum;
- (d) In case of difference of viewpoints on recommendations with the listed company, PAFs will have the option of either revising the report and issuing a revised report or

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<sup>102</sup> Para 1(f), Procedural Guidelines Circular, *supra* note 5.

<sup>103</sup> Para 1(c), 1(d) & 1(e), Procedural Guidelines Circular and Para 1(a), Modification Circular, *supra* note 5.

issuing its remarks in relation to the same - in either case, the same has to be issued as an addendum; and

- (e) Any factual errors and impending material revisions to be intimated to the clients within 24 hours of receipt of information and the material revisions to be communicated to the clients within 72 hours of receipt of information, ensuring that the client has adequate time to make informed decisions.

The prescribed methodology may raise following potential concerns:

- (a) Bilateral communication

The obligation to share reports simultaneously with the listed company encourages interactions between the listed company and the PAFs, thereby risking undue mutual influence. However, on the other hand, it can be argued that the requirement of sharing such communications as addendum to the clients creates transparency and ensures that the client is aware of conflicting positions. Further, this methodology also forces PAFs to share their report free of charge with listed company.

- (b) Verbal communication



It is unclear whether it will be permitted to receive clarifications/comments through in-person meetings or over telephonic communications, and whether such communication necessities being recorded as an addendum to the report (either as conversation transcripts or otherwise). It can be argued that such communications may not be permitted in order to avoid sharing of non-publicly available information or any mutual undue influence.

- (c) Factual errors & impending material revision v. comments & clarification

The Circulars<sup>104</sup> distinguishes between ‘factual errors and impending material revision’ and ‘comments and clarifications’, but they do not clarify the scope of these two categories of information received from the company. Comments/clarifications received from the company are required to be included in the addendum report if they are shared within the timeline provided by the PAFs. Information regarding ‘factual errors and impending material revision’ received from the company are required to be brought to the client’s attention within 24 hours of receipt of such information, and material

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<sup>104</sup> Para 1(c) & 1(e), Procedural Guidelines Circular and Para 1(a), Modification Circular, *supra* note 5.

revisions are required to be communicated within 72 hours of receipt of information, while ensuring that the client has adequate time to make an informed decision.

The Circulars do not provide flexibility to PAFs to not inform the clients regarding ‘factual errors and impending material revision’, even if they have been shared by the company after the time period provided to them to share their comments/clarifications. Further, the Circulars do not indicate whether an addendum to the report has to be issued in such a case, or whether communication in a manner acceptable to the PAFs would satisfy this obligation. Additionally, the threshold for determining materiality of such revision has been left to the judgment of the PAFs, which leaves room for potential difference of opinion with the company.

(d) Multiple reporting and timeline

Given the obligation of sharing the information regarding factual errors and material revisions with clients within the prescribed time,<sup>105</sup> in the event such information is shared by the company in multiple tranches, PAFs will have to issue multiple intimations to the clients – which may create confusion.

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<sup>105</sup> Para 1(c), Procedural Guidelines Circular and Para 1(a), Modification Circular, *supra* note 5.

Further, the obligation to ensure that the client has adequate time to make an informed decision is on the PAFs. The company on the other hand does not have any obligation of ensuring that such information is shared in an expedited manner. In the event there is a delay on the part of the company, PAFs may not have the benefit of the prescribed 72 hours to prepare the communication on material revisions.

(e) Rounds of rebuttal & sharing of addendum report<sup>106</sup>

It is unclear whether addenda to the report are required to be shared with the listed company. One can argue that the requirement of sharing the report simultaneously, extends to addenda as well. This raises further questions regarding whether the listed company has the right to share their comments on the addendum/ revised report; and if yes, whether multiple addendums have to be issued in such a scenario.

(f) Draft reports

It is unclear whether the obligation to share report simultaneously with clients and listed companies apply at the draft stage, if sharing such draft is a business

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<sup>106</sup> See Rabindra Jhunjhunwala & Saranya Mishra, *India: companies, know thy rights – the right to rebut proxy advisors and the right to redress*, INTERNATIONAL BAR ASSOCIATION (Sept. 25, 2020), <https://www.ibanet.org/Article/NewDetail.aspx?ArticleUid=AE1D1788-24DA-4E3F-9275-200703518E4E>.

practise of the PAFs. Given the obligation of share comments/clarifications as addenda as well as the requirement of simultaneous report sharing, it can be argued that SEBI does not encourage such practises.

(g) Prescribing time for comments

The timeline for receiving comments/clarification from the listed company is to be decided at the discretion of the PAF. In order to avoid subjective or preferential treatment of listed companies and promote transparency, PAFs may consider including a clear policy in this regard in the voting guidelines. The listed company has the option to disclose such clarification to the stock exchanges directly, if the PAF does not entertain delayed responses.

(h) Addressing difference of opinion on comments and clarification

As per the Circulars, PAFs are not bound to revise their recommendations in case of differences of opinion with the listed company on 'comments/clarification' received from the company. However, they will no longer have the option of not responding to such comments in the addendum report, provided they are received within the prescribed time.

## **5. Grievance redressal**<sup>107</sup>

The mechanism of grievance redressal provided in the Circulars is not available to PAFs in the event they are the aggrieved party. Further, the Circulars are silent on the manner in which the grievance redressal process will be implemented.

### **B. IMPACT ON LISTED COMPANIES**

#### **1. Right to be heard**

The Circulars have ensured that the listed companies have the right of being heard by PAFs and their clients, without having to make such clarification as disclosures to the stock exchange.<sup>108</sup>

#### **2. Grievance redressal**

The mechanism for grievance redressal, once the mechanism for implementation of the same is specified, will provide a formal channel for communication with SEBI for issues with PAFs.<sup>109</sup>

#### **3. Transparency and quality control**

The availability of the voting recommendation policy, the requirement of clarifying where standards higher than the prescribed

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<sup>107</sup> See Rabindra Jhunjhunwala & Saranya Mishra, *Id.*

<sup>108</sup> See Rabindra Jhunjhunwala & Saranya Mishra, *Id.*

<sup>109</sup> See Rabindra Jhunjhunwala & Saranya Mishra, *Id.*

legal standards are followed, disclosure of research methodology will ensure that PAF recommendations are not arbitrary.<sup>110</sup>

### C. IMPACT ON CLIENTS<sup>111</sup>

The mechanism proposed by the Circulars ensures sanctity and transparency of information flowing from the listed company to the clients, thereby helping clients make informed voting decisions. Further, the requirement of reporting errors to clients will help clients analyse their service providers i.e. the PAF's performance.

## V. CONCLUSION

Through this article, the author has highlighted the role being played by the fledgling PAF industry in the Indian corporate governance landscape and the necessity which SEBI realised in standardising their business practices. The analysis of the provisions of the Circular leads us to the deduction that SEBI chose to adopt a light-touch approach, instead of being overtly prescriptive or paternalistic in their manner of regulating this nascent and relatively small industry. Provisions of the Circular in relation to conflict of interest reinforce some of the existing position under the RA Regulations, with certain added clarifications. The issues which are

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<sup>110</sup> See Umakanth Varottil, *supra* Note 85.

<sup>111</sup> For Black Rock's comments to SEBI while drafting the 2019 Report, (Aug. 16, 2019), <https://www.blackrock.com/corporate/literature/publication/consultation-to-securities-and-exchange-board-of-india-on-issues-related-to-proxy-advisors.pdf> (Nov. 11, 2020).

left open-ended may lead to muddled waters for PAFs, until market forces settle such business practices. It is premature to answer the question whether the friction caused in this process, which had originally led to the review of this industry and 2019 Report, has been neutralised by the Circulars. Further, the introduction of the grievance redressal mechanism is a welcome addition. However, until clarity regarding its enforcement mechanism is available, it lacks lustre. It can be argued that time and market forces will likely clarify many of the concerns raised in this article, which seems to be SEBI's intention as well. Until such time, PAFs will have to navigate their way through these puzzlements to implement the standards prescribed by the Circulars.