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PROXY ADVISORY FIRM AND ITS LEGAL RECOGNITION IN INDIA

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Abstract

Proxy advisory firms (PAFs) play a vital role in guiding investors on voting decisions and strengthening corporate governance. In India, they are legally recognised under SEBI (Research Analysts) regulations, 2014, with additional norms issued in 2020 to ensure transparency and conflict free advice. While they enhance shareholders activism and accountability, PAFs face challenges such as corporate resistance, conflict of interest, and limited investor awareness. This paper highlights their Role, legal recognition, advantages and obstacles they encounter in India.

INTRODUCTION:

Corporate governance is a process of the company to make a smooth flow in the governess of the company and it helps to protect the interest of the shareholders and its compose the relationship between the management, board of directors and shareholders, Then It's ensures to maintain accountability and full transferability .it also helps to make a long term trust and good faith among the investors .so it helps to social and economic growth of the company. In India Proxy advisory firms grew after such corporate governance failures like **Satyam scandal (2009),** which highlighted stronger need of shareholders awareness, and created a pathway for a formation of proxy advisory firms. Then only the PAFs are formed in India. The PAFs are also recognized in SEBI under the **research analyst regulation, 2014.** The proxy advisory firm is a separate legal entity and it's registered under the companies Act, 2013 but it's regulated and registered by the SEBI.

The PAFs help the investor and shareholders in their voting rights as recommendation and manage the conflict of interest with the proper backed research. So, the proxy advisory firm

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acts as an intermediary for the company and the shareholders and they help the minority shareholders and investors in their right to vote, proxy voting, right to collect dividend and transferability of shares. The proxy advisory firm is expected to have significant growth in future as corporate governance become more globalized. PAFs push companies to adopt the higher ESG (Environmental, social and governance) standards. PAFs will play a key role in ensuring that businesses are not only profitable but also responsible and sustainable in future. In this research paper we are going to see about the PAFs role, legal recognition and the obstacles they faced in the Indian market.

REVIEW OF LITERATURE:

S. Subramanian (2016), Proxy advisory firm in India corporate ownership & control, 13, 2:

Which guide investors on how to vote in company meetings, started growing in India after SEBI’s 2010 rules on voting Disclosure. Globally, such firms help improve corporate governance, and in India, companies like InGovern, IIAS, and SES began this work. The industry has big growth potential due to India’s economy, pension reforms, and stronger governance laws, but it also faces hurdles like low investor awareness, pushback from companies, regulatory issues, competition, and staff shortages.

Debkanya naskar (2021), Regulating proxy firm in India, 4, 1:

The paper discusses the regulation of proxy advisory firms in India, which give voting advice to investors in company decisions. It explains how these firms support better corporate governance but also raise concerns about bias, conflict of interest, and accountability. SEBI has introduced rules to improve transparency, disclosure, and independence of these firms. The paper highlights both the benefits of proxy advisors—like protecting minority shareholders and the challenges, such as possible over-reliance on their advice and resistance from companies. It concludes that balanced regulation is needed to ensure these firms strengthen corporate governance without creating new risks.

David F. Larcker, (2014), outsourcing shareholder voting to proxy advisory firms, rock centre for corporate governance:

The paper explains how proxy advisory firms work, why they are important, and the issues around regulating them. These firms guide investors on how to vote in corporate matters, helping improve accountability and governance. However, concerns arise about their influence, accuracy, conflicts of interest, and the risk of investors depending too much on them. The study highlights the need for clear rules that ensure transparency and independence while still allowing proxy advisors to play a positive role in strengthening corporate governance.

RESEARCH METHODOLOGY:

In this research we adopt the doctrinal and qualitative approach and its relay on the primary and secondary sources for the proxy advisory firm and its legal recognition in India .in this study we refer the article and research paper that are mainly focused on the PAFs role, its legal recognition in India and its critical analysis in the issuing from 2014-2020. In this research we organise its legal recognition, role in Indian capital market and the critical analysis, the analysis isn't done in descriptive, it highlights the advantages and disadvantages of the proxy advisory firm in India.

RESEARCH OBJECTIVE:

1. To examine the Role of proxy advisory firm India.
2. To study the history and Legal recognition of proxy advisory firms in India.
3. To Critical analyse the advantages and obstacles of the proxy advisory firm in India.

HISTORY OF PAF IN INDIA:

Proxy advisory firm was firstly emerged in the united states in 1980s, It's created because in 1980s the US market is majorly done in the mutual funds like CALPERS(California public employee retirement system), they holds the major shares in most of companies for that they have corresponding fiduciary duty to vote in the shareholders meetings ,but they are lacked in the analysing and in that time during shareholder meeting not all the shareholders are able to attend it ,so it's needed that proxy voting.

To fill this gap the ISS (institutional shareholder service) was formed in 1985, created by "Robert monks". It is the first proxy advisory firm in the world. It's created to provide a recommendation in their fiduciary duty like voting rights and proxy voting they give recommendation only with the proper backed research about the companies. An Indian proxy advisory firm was introduced in 2010 by the impact of the "satyam scandal". After this only the SEBI realized that the shareholders and investors needed the help .In India the PAFs is a separate legal entity but it must be registered and regulated by the SEBI.

PROXY ADVISOR:

Proxy advisor is an organisation or a firm that helps the investors and shareholders by giving recommendation in their voting rights, proxy voting policies, advising and giving them education and training about the field, all backed by the well-versed research about the company. The term proxy advisor was clearly defined under the SEBI (securities and exchange board of India) regulations, 2014 under 2(p), as

"Any person who provides the advice, through any means, to institutional investors and shareholder of the company, in relation to exercise of their rights in company including recommendations on public offer or voting recommendation on agenda items"

The proxy advisors are mainly regulated by the SEBI and they give the" procedural guidelines" for the proxy advisors on August 3, 2020.

LEGAL RECOGNITION IN INDIA:

In India the proxy advisory firm was initiated by the satyam scandal case because this case shows the great corporate governance failure. This will become the gateway for the PAFs in India to produce the individual shareholder and investors. So SEBI came up with this firm. In India the "In-govern research services (2010)" was the first proxy advisory firm and by 2010 IIAS was operated in India and helped the individual shareholders and investors. In 2014 SEBI brought the proxy advisory firm into the SEBI regulation and gave them the recognition of "registered research analysts".

The PAFs must be registered in SEBI. The SEBI is a main board that regulates the PAFs in India. In 2020 SEBI Came up with the strict rule about their transparency, accountability and fairness, the rules are:

1. Mandatory annual review for the voting recommendation

2. Disclosure of research methodologies and processes

3. Timely communication of errors to client and companies

4. Procedure for managing and disclosing conflicts of interest.

Example:

1. In-govern research services (2010):

It was the first proxy advisory and corporate governance research firm. It was set up in 2010.Shriram Subramanian was the founder of this firm. This firm's functions are giving voting recommendations, conducting the corporate governance research and publishing the reports of the governance of listed companies in India.

2. Institutional investor advisory service (IIAS) (2010):

It was founded in 2010 .it was set up by industry proffesionals.it and was one of the largest and most influenced proxy advisory firms in India. It was not only focused on voting recommendation it's also focused on policy advising and ESC reports. It was founded in 2012 and it was an independent and research focused firm. Its main aim is to protect the minority shareholders right and prioritizing transparency in disclosures. It came up later but with a more investor protection approach.

ROLE OF PAF:

Proxy advisory firms play a vital role in corporate governance. They also provide the following

1. Voting recommendation:

The primary role of the proxy advisory firm is that they are recommending voting for the individual shareholder and investors by the well-versed research made by the firm. And they also properly analyse the resolutions of the company from its resolutions and give the recommendation for the shareholders' individual voting. They only analyse MOA when there is any change in business and objective and the AOA is analysed when there is a governance or voting changes unless and otherwise they didn't analyse it.

2. Proxy voting:

Proxy voting is the process shareholder delegate his voting right to the another person when they are unable to attend the board meeting, It's also done under the recommendation of the proxy advisory firm .the person who done the proxy voting is called as proxy and he act as agent for the shareholder but his rights will be limited only with the voting not having the rights to speak like an agent unless the articles of association allows.

3. Shareholder awareness:

The proxy advisory firm plays a great role in the well versed research about investors. The PAFs are also providing education and training to the shareholder and investors for the betterment of their choices in voting and helps to improve corporate governance. The training helps to understand the governance and make them use their rights effectively, so the PAF gives training and education to the shareholders and investors.

4. Policy advisors:

Another important duty of a proxy advisory firm is to give policy advising to the investors for their better of life. In these the PAF acts as a policy advisor. They give advice among the SEBI,MCA and stock exchange .Then they give the advice among the issues and disclosure of voting rights and giving advice among their investment by this they only represent at that regulatory level not in companies meeting.

CRITICAL ANALYSIS:

a) Advantages:

1. Accountability:

In India proxy advisory firms are regulated by the SEBI so they must be registered under the SEBI regulations. They must give transparency among its recommendations. Like, PAFs must give a proper reason for every voting recommendation. And they must ensure that they give independent, unbiased and well verse recommendations.

2. Proxy voting (fiduciary duty):

Proxy voting means that the shareholder gives permission to another person to attend the meeting behalf of himself. The person called as proxy. So it helps shareholders to take part in the company’s activities without a physical present. They must carefully fulfil their fiduciary duty, because the proxy acts like a trustee to the shareholder and only acts for the benefit of the shareholders. If the shareholder gives clear direction they must be beside it but there is no direction by shareholders they must exercise it independently with carefulness.

3. Voting recommendation:

The main advantage of the PAFs are independent voting recommendations because not every shareholder has a time to analyse or make well versed research about the companies document like MOA, AOA and resolution so the PAF makes the research and gives the fair and independent voting recommendations. It will ensure better corporate governance and develop the minority shareholders.

4. Cost effective solution:

The PAFs are a more cost-effective solution because if you hire any individual financial expert it's more costly and consumes more time. So, the PAFs are more cost and time effective. The PAFs are more beneficial to the minority shareholders because they cannot afford the costly consultations. Their quick decision making helps a shareholder vote wisely and is less expensive.

5. Improve standard of company/business:

The PAFs also increase the company’s standards by promoting transparency and accountability. Because the company promotes the standard of companies individual shareholders and investors by giving them an proper education and training and also giving them an proper advise by the well versed research done by them so they indirectly improve the standard of the company by improving the standard of their individual shareholder and investors, and promote the corporate governance, strengthen the long term goals and investors trust among companies.

b) Disadvantages:

1. Lack of transparency:

In the voting and investing recommendations the proxy advisory firms only disclose the recommendation for that they don't disclose the research report clearly. If the PAFs give the recommendations for the company they rate without proper disclosure of the report the shareholder doesn't know it's biased or not. If the methodology and reasoning aren't transparent it's difficult to make the PAFs accountable when their recommendations turn out to be harmful.

c) Lack of awareness:

Lack of awareness is one of the main disadvantages of the proxy advisory firms because many small retailers and investors aren't fully aware of the PAFs and PAFs mainly use technical language in reports so it makes it difficult to understand for most common investors. If only big institutional investors are well known about the PAFs so the small investors are excluded. This will create an imbalance in shareholder participation and weak corporate governance.

d) Biased activities:

Some proxy advisory firms are not only giving recommendations to the individual shareholder and investors they are also giving consultations for the same company so, the recommendation given by the PAFs has the risk of being biased. PAFs also feel pressure to maintain a good relationship with the influenced & big companies so they may give recommendations in favour of them in these cases also there will be the risk of bias.

e) Reduce discretionary power of BOD:

The main power of the board of directors is managing the company's affairs. When the proxy advisory firm gives recommendations about voting and investment it will affect the discretionary power of BOD. When the PAFs are dealt with short governance like voting, ESG policies and mergers. The BOD is pressured to make a long term governance so it will cause the board to please the shareholder instead of imposing policies.

f) No uniform methodology:

Every proxy advisory firm has its own parameters and assumptions for analysis in companies so it will create an inconsistency among companies. Since there is no regulation for the methodology it will create a major inconsistency so there is no uniform methodology.

SUGGESTIONS:

Based on the analysis proxy advisory firm in India, several measures can be suggested to strengthen their role and creditability. Firstly, in India there is a lack of awareness among the small retailers and shareholders about their rights and the importance of informed voting. So, the program about the PAFs can give more awareness to minority shareholders and investors about the performance of PAFs. Also, there are no clear provisions for PAFs in SEBI. So, The

SEBI can make more clarity in the regulations about the PAFs in India. In India judicial recognition of PAFs are limited so the government can give more recognition to the PAFs in India. They can also contribute to the development of future professionals and researchers by Giving practical training to the students and encourage more academic research about the PAF.PAF should act as a mediator to ensure the decisions are transparent and accountable while protecting shareholder rights and Balance the powers of both PAFs the discretionary power of BOD.

CONCLUSION:

Proxy Advisory Firms (PAFs) in India play a vital role in improving corporate governance and protecting the interests of shareholders. In particular, they help minority shareholders exercise their rights such as voting rights, participation in general meetings, receiving profit distribution and transferring shares. These firms have been given statutory recognition through SEBI Regulations 2014. Later, strict guidelines were introduced in 2020 to ensure transparency, fairness and avoidance of conflict of interest. Through this, PAFs act as intermediaries providing reliable information and advice to investors.

However, there are several challenges: Lack of transparency, Low investor awareness, sometimes biased advice and Reduced power of the board of directors, Lack of consistent procedures. Therefore, for PAFs to deliver their full benefits, the Indian capital market needs: More robust regulation, judicial recognition, Investor awareness programs, Practical training and education, In-depth education and research. Therefore, proxy advisory firms have great potential to grow significantly in India and become a powerful tool for promoting corporate accountability and transparency. This will contribute significantly to investor confidence, sustainable growth of companies and economic growth. At present proxy advisory firms are globally considered as advisory's, not policymakers.

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