"ACGA White Paper on Corporate Governance in India"

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ACGA takes full responsibility for the accuracy of this paper and any errors contained in it are our own.

Jamie Allen
Asian Corporate Governance Association, Hong Kong
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Executive Summary & Recommendations

The "ACGA White Paper on Corporate Governance in India" is the first initiative of its kind written with the collaboration of major investors and other market participants based both in India and around the world. It was compiled by ACGA during 2009, mostly in the latter half of the year, and is based on detailed research and wide-ranging interviews.

The aim of the "India White Paper" is to provide officials, financial regulators, listed companies, investors and others with constructive and detailed suggestions for the broadening and deepening of sound corporate governance in India. While India has undertaken numerous reforms in corporate governance over the past decade, especially in the area of company boards, independent directors and disclosure and accounting standards, certain critical areas remain to be addressed—particularly relating to the accountability of promoters (controlling shareholders), the regulation of related party transactions, and the governance of the audit profession.

We believe that reforms are needed in these areas to strengthen the integrity of India's capital markets and to enhance its goal of becoming an international financial centre. We also believe that improvements in these areas should not be delayed for too long.

Accordingly, this White Paper focuses on, and makes recommendations with regard to, five key issues:

- Shareholder meetings and voting
- Related-party transactions
- Preferential warrants
- Corporate disclosure
- The auditing profession

Each of these issues is considered significant in this paper and the order in which they appear should not be read as implying some are more important than others. The paper starts with a discussion of the accountability of shareholder meetings and voting processes because this is an immediate and growing area of concern for many global institutional investors who are voting their shares in India. It is also an issue that is capable of being addressed quickly and efficiently by companies and regulators, if they so desire.

The absence of a corporate governance issue from this paper, most notably the challenge of creating an effective and independent board of directors, does not mean that ACGA and its members are less interested in it or how it is developing in India. On the contrary, the role of the board and the effectiveness of directors are of paramount concern to the Association. It is not addressed in this paper because a great deal has been written on the subject in India over the past decade and the aim of this White Paper is to offer fresh perspectives on newer issues.

A summary of the five issues and our key recommendations follows:

1: Shareholder Meetings and Voting

Shareholder meetings and proxy voting processes in India—like many parts of Asia—lack efficiency and accountability. Voting processes need to be modernized to reflect best market practices and the growing global interest in active shareownership. We recommend that companies implement the following measures:

1.1 Ensure that the quality, transparency and reliability of shareholder meeting agendas is sufficient to allow responsible investors to make informed voting decisions on each resolution.

1.2 Post the meeting notice (final agenda) and explanatory notes (detailed circular) for all general meetings, both annual and extraordinary, on the company website as well as on the websites of both exchanges.

1.3 Ensure that the notices are easy to find (eg, they are prominently displayed on company websites and/or within an investor relations section).

1.4 Archive notices for 10 years on both the company website and on the exchange websites.

1.5 Release meeting notices and explanatory notes at least 28 days before annual general meetings.

1.6 Conduct voting on all resolutions at AGMs and EGMs meetings by a poll. Engage an independent scrutineer to count and audit the vote.

1.7 Allow proxies to speak at meetings, irrespective of whether the company law is amended on this point.

1.8 Publish full voting results on the company website and on the exchange websites within 24 hours of the meeting.

We also recommend that SEBI encourage the top 100 listed companies in India to start voting by poll as soon as possible.

2: Related-Party Transactions

India has a notably weak regime governing related-party transactions. Regulation needs to be overhauled and minority shareholders accorded much greater protection. We recommend that the government and regulators:

2.1 Introduce much stricter regulation on related-party transactions, including giving independent shareholders the powers to approve large transactions above a certain limit and enhancing disclosure requirements on other material transactions. Such regulation could be provided for in both the Listing Agreement and new SEBI regulations or guidelines.

2.2 Require the appointment of an independent financial advisor and an independent board committee to determine whether material transactions are fair and reasonable to all shareholders.

2.3 Require independent directors to exercise their duties more diligently and protect the interests of minority shareholders, especially in cases where the majority shareholder is also the manager of the company. Some degree of legal liability could be considered for directors in cases such as Satyam.

2.4 Encourage listed companies with numerous related transactions to set up a related-party transaction committee of their board. This would scrutinise such transactions, recommend to the board if shareholder approval should be sought, advise on disclosure and judge the fairness of transactions.

3: Preferential Warrants

The scope for the misuse and abuse of warrants in India is considerable. Regulation of their issuance to promoters needs to be tightened. We recommend that:

3.1 The issuance of preferential shares, warrants or other securities to promoters and other connected persons be prohibited (as in other markets), except under the limited circumstances envisaged in markets such as Hong Kong (ie, where the securities are part of a pro-rata entitlement made available to all shareholders on an equal basis, or as part of a shareholder-approved stock option scheme).

3.2 Companies be required to seek shareholder approval at their annual general meetings for the issuance, over the subsequent 12 months, of any new shares at a discount to a limited group of (non-controlling) shareholders. Strict rules should govern the size and discount of such offerings.

3.3 Listed companies review the way they use warrants and limit their application to forming part of a wider issue of debt or equity securities (ie, where warrants act as sweeteners for investors).

4: Corporate Disclosure

The scope, depth, timeliness, consistency and formatting of corporate financial disclosure in India could be greatly improved among listed companies. We recommend that:

4.1 The rules relating to the publication deadlines for audited annual results (and annual reports) be clarified for companies that opt to produce an unaudited fourth quarter report (with a limited review by the auditor). All companies should be required to produce audited annual results within three months and their full annual report within four, or at most five, months.

4.2 The format of quarterly P&L statements be reviewed to require additional details on revenues.

4.3 Listed companies be encouraged to provide both cashflow statements and balance sheets with their quarterly reports.

4.4 SEBI actively consults investors in both India and overseas regarding the format and content of balance sheets, P&L statements and cashflow statements, with the aim of making them more user friendly.

4.5 Stock exchanges (NSE and BSE) become the central depository for all listed company reports, announcements, circulars and notices, and that such information be archived for 10 years.

4.6 Companies use their websites more efficiently and as a stronger communications tool for investors and other stakeholders.

4.7 CorpFiling and EDIFAR be merged into one database, with the structure following the organisation of EDIFAR, but with further thought being given as to how information could be even more easily accessible.

5: The Auditing Profession

The Indian auditing profession is highly fragmented. It would benefit from some consolidation as well as an independent audit regulator. We recommend that:

5.1 Chartered accountant (CA) firms be allowed, and encouraged, to consolidate.

5.2 Artificial caps on the number of audit trainees and audit partners be removed.

5.3 The Government establish an independent regulatory body for the audit profession. Such a body could draw its talent from among the many experienced auditors in India, including those who have worked overseas.

5.4 The SEBI Board approves SCODA's recommendations on the mandatory rotation of audit partners and the clarification of the audit committee's responsibilities regarding auditor independence.

5.5 The Government and the securities regulator proactively consult institutional investors and other market participants in India and overseas as they move forward on any reform of the audit profession.

Introduction

Few would dispute that the scale and scope of economic reform and development in India over the past 20 years has been impressive. The country has opened up large parts of its economy and capital markets, and in the process has produced many highly regarded companies in sectors such as information technology, banking, autos, steel and textile manufacturing. These companies are now making their presence felt outside India through global mergers and acquisitions.

A lesser known fact about India is that in April 1998 the country produced one of the first substantial codes of best practice in corporate governance in Asia. It was published not by a governmental body, a securities regulator or a stock exchange, but by the Confederation of Indian Industries (CII), the country's peak industry body.

The following year, the government appointed a committee under the leadership of Kumar Mangalam Birla, Chairman, Aditya Birla Group, to draft India's first national code on corporate governance for listed companies. Many of the committee's recommendations were mandatory, closely aligned to international best practice at the time and set higher governance standards for listed companies than most other jurisdictions in Asia. The Indian Code of Corporate Governance, approved by the Securities and Exchange Board of India (SEBI) in early 2000, was implemented in stages over the following two years and led to changes in stock exchange listing rules, notably the new Clause 49 in the Listing Agreement.

Further reforms have been made over the past decade to modernise both company law and securities regulations. The Companies Act, 1956 has been amended several times, in areas such as postal ballots and audit committees, while committees were appointed in 2002 and 2004 to recommend improvements. The latter committee, chaired by Dr J.J Irani, was charged with undertaking a comprehensive review of the 1956 Act and its recommendations led to a rewrite of the law and a new Companies Bill, 2008. (This bill was resubmitted as the Companies Bill, 2009 following national elections in 2009. It is still waiting to pass Parliament.)

In the area of securities regulation, SEBI has made numerous changes in recent years including: revising and strengthening Clause 49 in relation to independent directors and audit committees; revising Clause 41 of the Listing Agreement on interim and annual financial results; and amending other listing rules to protect the interests of minority shareholders, for example in mergers and acquisitions.

Not surprisingly, the Satyam fraud of late 2008 led to renewed reform efforts by Indian authorities and regulators. SEBI brought out new rules in February 2009 requiring greater disclosure by promoters (ie, controlling shareholders) of their shareholdings and any pledging of shares to third parties. And in November 2009 it announced it would be making some further changes to the Listing Agreement, including requiring listed companies to produce half yearly balance sheets.

More recently, in December 2009, the Ministry of Corporate Affairs (MCA) published a new set of "Corporate Governance Voluntary Guidelines 2009", designed to encourage companies to adopt better practices in the running of boards and board committees, the appointment and rotation of external auditors, and creating a whistleblowing mechanism.

The Guidelines were developed through a process of “stakeholder consultation” and drew upon papers published slightly earlier by a task force of the Confederation of Indian Industries and another from the Institute of Company Secretaries of India.

Despite these wide-ranging developments in regulation and policy, what becomes increasingly apparent in India is that the reform process has not addressed, or effectively addressed, a key challenge at the heart of the governance problem, namely the accountability of promoters to other shareholders. Even though most listed companies have large controlling shareholders, typically a family, the regulation of related-party transactions in India is minimal. Promoters have considerable freedom of action in undertaking such transactions and are subject to only limited regulatory controls. They are also permitted to issue preferential warrants to themselves at an effective discount to the market price—something that would not be condoned in more developed markets.

In this context, relying largely on independent directors (appointed by controlling shareholders), independent board committees and greater corporate disclosure as the primary mechanisms to check abuses of power by promoters and to safeguard the interests of minority shareholders is likely to prove weak and insufficient (as indeed it did in the Satyam case). Board reform is fundamentally important, and is a major issue of concern to institutional investors, but it needs to be complemented by other regulations that directly address the relationship between controlling and minority shareholders—in other words, a proper regime for the regulation of related-party transactions.

While some leading Indian companies deserve credit for actively pursuing high standards of governance, including producing examples of world-class corporate disclosure, the strong growth of the economy and capital markets has fostered, in our view, a fair degree of complacency towards corporate governance and the rights of minority shareholders. As this paper shows, few listed companies in India are attuned to a major global trend of the past five years—the expansion of cross-border proxy voting—nor do they seem interested in voluntarily enhancing the transparency and fairness of their annual general meetings (eg, by fully counting all votes through a “poll”, rather than conducting voting by the old system of a show of hands). This complacency is also reflected in the ongoing difficulties that investors face in deciphering the financial statements of some listed companies, including even some large caps.

For these reasons, we believe that a more comprehensive review of corporate governance regulation and practices is required in India. While the new “Voluntary Guidelines 2009” provide helpful and detailed guidance to companies interested in developing a more effective board of directors, they do not address many of the issues raised in this White Paper (with the exception of a brief reference to the rotation of auditors). Nor will the new Companies Bill resolve these challenges.

The aim of the “ACGA India White Paper” is to provide officials, financial regulators, listed companies, investors and others with constructive and detailed suggestions for the broadening and deepening of corporate governance in India. We believe that the paper’s recommendations, if implemented, would considerably strengthen the integrity and competitiveness of India’s capital markets, safeguard the legitimate property rights of investors, and enhance the country’s goal of turning Mumbai into international financial centre.

Issue 1: Shareholder Meetings and Voting

Shareholder meetings and proxy voting processes in India—like many parts of Asia—lack efficiency and accountability. Voting processes need to be modernized to reflect best market practices and the growing global interest in active shareownership

A modern trend

Although voting at company meetings is a basic shareholder right under company law, until recently it received limited attention in many parts of the world, including Asia. This situation has been changing rapidly as institutional investors come under increasing pressure to vote their shares as a result of regulatory pressure, market expectation or because they view voting as an important fiduciary duty. This was a trend that ACGA highlighted in our "Asian Proxy Voting Survey 2006".

While comprehensive data on the volume of voting in Asia is not available, anecdotal evidence points to a significant increase across the region over the past five or more years. Large European and North American pension funds have long voted in Japan, since that has been their biggest Asian market for investment and the country has an active proxy solicitation industry.[1] But these same investors are now voting more actively in other Asian markets, especially Hong Kong, Korea, Singapore, Taiwan and Thailand.

Evidence of the growing global interest in voting is reflected in the number of corporate governance and proxy voting policies published by major pension and investment funds in Asia, Canada, Europe, the UK and the US.[2] Some of these documents have been tailored for Asia, or take into account specific local issues.

Voting in Asia is not a preserve of foreign investors only. Several state pension funds, such as the National Social Security Fund in China, the National Pension Corporation in Korea, the Employees Provident Fund in Malaysia and the Government Pension Fund in Thailand, all have voting policies and are voting in their respective markets.

Nor is the trend limited to the state: Japan's Pension Fund Association (PFA), a private body, began promoting proxy voting in 2001. The PFA became involved after its investment returns turned negative in 1999 and, in order to improve returns and the governance of companies, it developed a set of voting guidelines and began actively voting its own shares.[3]

On the rise in India

Since India is a newer market for foreign institutional investors (FIIs), their degree of voting at local annual meetings is somewhat more limited than in other Asian markets. However the evidence suggests that foreign investors are taking voting more seriously. "This year (2009) I could see many more FIIs participating in meetings and casting their votes. The trend in blue-chip companies, where FII holdings is high, (shows that) the participation rate is always high during the past few years," said a manager at a large sub-custodian bank in Mumbai.

Indeed, the volume of voting in India is likely to rise in tandem with greater foreign investor participation in India and a stronger focus on voting globally. According to data from the Securities and Exchange Board of India (SEBI), the financial market regulator, the participation of foreign investors in Indian equity markets began increasing in 2005

and picked up momentum in 2006. Although the level of FII investment dipped somewhat in 2007/8 and 2008/9 as a percentage of total market cap, it has risen again over the past eight months (see table below).

Year	FII investment as % of market cap
2005-06	15%
2006-07	15.4%
2007-08	14.3%
2008-09	12.7%
2009-10 (Apr - Nov)	13.4%

Source: SEBI Bulletin, November 2009 and August 2008.

Antiquated systems

Although shareholder voting may seem like a straightforward activity, or should be, voting systems in many countries can be surprisingly archaic and complicated—especially for cross-border investors. ACGA's "Asian Proxy Voting Survey 2006" highlighted the key problems as being:

- **Quality of information:** Listed companies often provided insufficient information for investors to make informed voting decisions (eg, detailed meeting circulars and annual reports were not ready by the time foreign investors had to cast their votes, or final meeting agendas lacked key details on resolutions).

- **Vote counting:** A lack of "voting by poll", which is the full counting of all votes cast. Many markets still voted by a show of hands or a variant such as voting by "acclamation" (where the chairman calls for shareholders to shout their support or opposition) or voting by "assent" (where the chairman simply asks if everyone agrees). Voting by poll is the only fair and transparent system.

- **Publication of AGM results:** An absence of detailed voting results being published after shareholder meetings. Only voting by poll, again, is capable of producing a complete set of transparent, quantitative results.

While progress in modernising voting systems is apparent in many markets since 2006, most notably China, Hong Kong and Thailand, and to a lesser extent Japan, the situation in India remains problematic. The key obstacles that institutional investors face in India could be classified into three types:

- Access to full meeting notices
- The counting of votes at meetings
- Voting results not being published

Meeting notices: not easy to find

Detailed agendas for annual shareholder meetings are often not easily accessible in India, or not as accessible as in other Asian markets. Many companies, including blue chips, do not upload these documents to the websites of the two main stock exchanges, the Bombay Stock Exchange (BSE) and the National Stock Exchange (NSE), nor do they make them clearly available on their own websites.

A common practice in India is to print the final AGM agenda and insert it as a separate sheet into the company annual report, which is then posted to shareholders. Company secretaries interviewed by ACGA admit that the AGM notice sometimes does not reach shareholders because the annual report may be lost in the mail or the notice may not have been put in the report.

One executive interviewed said that if investors did not receive the agenda with the annual report, they could always call the company and ask for another to be sent. While this solution may help retail shareholders, it is unlikely to be workable for domestic or foreign institutional shareholders that vote at hundreds or thousands of AGMs and must meet early voting deadlines set by custodian banks. (Note: While company law in India and elsewhere usually allows shareholders to vote by proxy up to 48 hours before a meeting, global custodian banks typically set deadlines of eight to 10 days before meetings for the receipt of votes from global investors.)

A better practice, followed by some of the large-cap companies listed in the table on page 15**,** is to include the AGM agenda and explanatory notes as part of the content of the annual report itself. While this resolves the problem of insertions falling out of annual reports, it is not entirely satisfactory either. As the table shows, there may be a delay in the publication of annual reports, and few companies announce in advance when they plan to publish them.

It is evident that many listed companies do not yet see the need to make their AGM agendas consistently and quickly available online. While companies often have dedicated investor relations sections on their websites—devoted to the dissemination of financial reports, investor presentations, company IR contacts, other shareholder information and company announcements—there is rarely a calendar of events explaining when the AGM will be held, a copy of the meeting agenda and, following the meeting, any disclosure of voting results (even in summary form). Two exceptions are the Housing Development Finance Corporation (HDFC) and Infosys, both of which published their 2009 AGM agendas on their websites.

Inconsistency is also apparent in the archiving of AGM agendas. Companies that insert printed sheets into the hard copies of their annual reports do not archive these notices on their websites. Some companies, including Reliance Industries and the Steel Authority of India (SAIL), archive their agendas indirectly by providing copies of past annual reports (which contain the notice) on their website. Others, such as Kotak Mahindra and Tata Consultancy Services, archive their annual reports, but not all of them contain AGM notices. Tata Consultancy Services' 2007-08 annual report included its AGM agenda, but its recent 2008-09 report did not.

Since the uploading of notices on the websites of the two exchanges is rare, so is the archiving of them. AGM agendas that are posted on exchange websites will be archived

for five years. But, as a senior official of a local custodian bank stated, "Only 10% of the notices are available on the company/stock exchange website, the remainder are received as hard copies, which are scanned and forwarded to clients".

It is worth pointing out that in major markets around the world the archiving of meeting notices on exchange websites is becoming a common practice. It allows investors to understand the corporate actions undertaken by listed companies in the past, what governance standards they applied in major transactions (eg, new fund raising or acquisitions), who they nominated to their board of directors, and whether the conduct and content of meetings showed any improvement in governance practices and awareness of shareholder rights.

All in all, it takes far longer than it should to search online for AGM agendas of listed companies in India. It is like looking for a needle in a haystack, since it can take up to 45 minutes to check the two exchange websites and then, not finding anything, to search a poorly organised company website. On occasion, the full notice might be provided on the BSE, but not NSE, website or vice-versa. Meanwhile, some US-listed Indian companies provide their meeting notices to the Securities and Exchange Commission website, but not to the NSE or BSE.

Given India's reputation for information technology, and the pride that its large companies take in their governance initiatives, it seems odd that more use is not made of the exchange websites. A senior executive at one of the exchanges said there were some back-end IT issues that prevented listed companies from seamlessly uploading notices to its website. One problem is that many meeting notices inserted into annual reports are not prepared on computer, hence cannot easily be converted into PDF format. (One simple solution would be to scan the documents.) However, this explanation cannot account for the behaviour of the large-cap firms.

In 2008, the NSE said[4] that it was working on a solution to this problem and, in 2009, a number of companies started to post full EGM (but not AGM) notices on one or both of the exchange websites. One was RS Software, which called an EGM for January 13, 2009 and earlier posted its full notice on the BSE website on December 17, 2008. Others include the Union Bank of India and PTC India, a public-private partnership initiated by the Indian government to be a provider of power trading solutions in India**.** Yet the availability of AGM notices remains noticeably lower.

As the shareholder base and capital markets in India become more international, the pressure on companies to use websites to communicate meeting information with shareholders is likely to grow. The way in which companies run their meetings could well become a litmus test of their governance culture and attitude towards shareholders.

Company	Date of 2008 AGM	Availability of 2008 AGM agenda & detailed notes	Date of 2009 AGM	Availability of 2009 AGM agenda & detailed notes
Reliance Industries	June 12	Only in annual report on website. Not on BSE or NSE website, or separately on the company's website.	Nov 17	AGM date announced on BSE/NSE websites on October 16, but no detailed agenda. However, annual report uploaded on website with detailed notice on Oct 7.
Oil & Natural Gas Corp (ONGC)	Sept 19	As above for Reliance.	Sept 23	Annual report uploaded onto website after AGM finished – notice published on August 10, 2009
Bharti Airtel	Aug 1	Not available	Aug 21	Put on BSE / NSE websites on July 23, 2009. But notice dated April 29, 2009.
NMDC	Aug 8	AGM date announced on BSE / NSE websites on July 14, but no detailed agenda.	Aug 29	AGM date announced on BSE / NSE websites on July 31, but no detailed agenda.
Infosys Technologies	June 16	Notice and agenda on company website. Not on BSE or NSE websites.	June 21	Same as for 2008.
State Bank of India	June 24	Date of AGM given in CG report in annual report, but no full notice.	June 20	Date, time and venue on BSE / NSE websites, but no full notice.
DLF	Sept 30	Full notice and agenda only in annual report on its website. Not on BSE or NSE website.	Sept 30	Date posted on BSE and NSE on September 10. Full notice and agenda in its annual report on the company website.
Kotak Mahindra	July 28	Notice posted only on NSE website on June 25. But notice is dated May 9, 2009.	July 28	Not available. Unlike 2008, it did not post notice on the exchange website. But also not available on the company website or in its annual report.
Wipro	July 18	Included in the annual report and posted separately on website.	July 22	Not available. Unlike 2008, it did not post its notice in its annual report or on website.

Source: ACGA research

How are votes counted at AGMs?
A second major challenge at shareholder meetings in India is the way in which votes are counted—usually by a "show of hands" rather than by a "poll".

Voting by a show of hands disenfranchises investors since each person at a meeting, whether they are a shareholder or a proxy for a shareholder, gets one vote per resolution. It does not matter if they have 100 or 1,000 or a million shares, their voting power is equal. The unfairness is compounded for any shareholders voting by proxy (ie, those who cannot attend the meeting in person and must send in their votes beforehand), since there is a good chance they will have appointed the chairman of the meeting as their proxy (the default option in many countries) and that the chairman, having received multiple instructions to vote both "for" and "against" on each resolution, will do nothing.

Global institutional investors must invariably vote by proxy, since they typically own stakes in hundreds, if not thousands, of companies around the world. Geographic distance and the clustering of AGMs during similar months of the year in different countries make attendance in person difficult.

Not only is voting by a show of hands the standard practice at company meetings in India, but investors are further marginalised because companies enforce to the letter an archaic piece of English company law that says that proxies are not permitted to:

- Speak at meetings; or
- Vote on a show of hands (they can only vote on a poll).[5]

Since polls are rarely called at AGMs in India, this means that the proxy votes of shareholders who cannot attend meetings are not counted. This is arguably worse than other markets in Asia where voting by hand is the norm, such as Malaysia or Singapore, since at least in those markets a shareholder could ensure they get at least one vote per resolution by sending along a trusted associate as their proxy representative. In those markets, it is also possible for proxies to speak at meetings.

In theory, it should not be too difficult for a proxy, or group of proxies, to call for a poll in India. According to Section 179 of the Companies Act, "any member or members present in person or by proxy" may call for a poll if they hold shares in the company giving them not less than 10% of "total voting power" or on which the aggregate sum of not less than Rs50,000 (US$1,054) has been paid up.[6] While the first criteria could present some problems, the latter is not onerous.

In practice, however, the system is more complicated. As the following accounts from three Indian sub-custodian banks and one foreign investor illustrate, having a proxy call for a poll is often far from straightforward (and partly because some sub-custodian banks will not do so).

The first bank said that it sorted through the proxy votes from institutional investors manually and put the results in sealed envelopes for each company AGM. These envelopes are then given to "proxy agents"[7] who attend the meeting on behalf of the sub-custodian bank. (Custodian banks rely on these agents because the country's landmass is large and AGMs are sometimes held in remote locations, as that may be

where a company's registered office is located.) The agent is instructed to open the envelope at the meeting only if a poll is called. Since polls are almost never called, the envelopes are rarely opened. Yet the agents are not allowed to call for a poll, because that is against the bank's policy. (The bank said it believed that other sub-custodian banks followed the same policy.) Once the meeting is over, and if a poll has not been called on any resolution, the envelope will remain sealed and thrown away.

The two other banks also said they collated votes manually and put them in sealed envelopes to give to agents. Unlike the first bank, their agents were allowed to open the envelopes in order to know how to vote. While both banks claimed their agents were authorized to call for a poll, this has yet to be tested since no investor has asked for one. One of the banks stated that if a client sent any instructions of a sensitive nature, a bank official would go to the AGM instead of a proxy agent.

The third bank also noted that the chairmen of some companies were "increasingly calling for a poll on special resolutions". This fact cannot be corroborated, however, since the results of any votes by poll at AGMs do not have to be published on either the company's website or one of the exchange websites.

Not surprisingly, arguments are put forward by listed companies in India as to why voting by poll is "unnecessary and impractical". Some large companies, such as Reliance, are said to have far too many shareholders to make voting by poll feasible and cost-effective. The Companies Act says that voting shall be by a show of hands unless a poll is demanded—hence there is no need to change. And investors can only vote on "ordinary" matters at AGMs, such as the re-election of directors, the re-appointment of the auditors and the audited accounts for the year, while "important" matters are voted on by postal ballot[8], allowing investors to have their shares counted on issues of significance.

ACGA would respond to each of these points as follows:

- Communication technology exists that is capable of resolving the problem of hundreds or thousands of people attending a company meeting and voting by poll (ie, handheld wireless voting devices). The more such technology is used, the more costs should fall. In any case, a large shareholder base should not become an excuse for delaying reforms to vote counting. Any suggestion that such companies should be given an exemption from voting by poll would not be fair to other listed companies. And trying to define a bright-line test on what "large" means is likely to prove contentious and difficult.
- The Companies Act stipulations on voting by show of hands are, for the reasons given above, no longer as relevant as they used to be. Company law is often amended when it falls behind market or economic changes.
- To say that "ordinary resolutions" at shareholder meetings are unimportant is surprising. Voting for directors, for example, is an important aspect of the annual meeting and likely to become more significant in future.

Encouraging voting by poll

In 2008, British Columbia Investment Management Corporation (bcIMC), a large Canadian pension fund and ACGA member, decided to write to Indian companies in

which it invests and inform them that it intended to cast its votes by proxy. It also asked its custodian bank to ensure the proxy votes were cast by:

- Submitting the vote if, in addition to a show of hands, a poll was called; or
- Requesting a poll at the meeting if the chairman did not call for one.

The responses from four leading companies were briefly as follows:

Company	Response to bcIMC
Infosys	Infosys quoted the Companies Act, stating that voting was always by a show of hands unless a poll was demanded.
HDFC	HDFC also quoted the law, stating that it believed that not only did it comply with the regulations, but also the "spirit of the regulations".
Reliance Industries	RIL gave a rather vague response stating that it would serve its shareholders "in the best possible manner subject to the applicable statutory framework".
Bharti Airtel	Bharti quoted the Companies Act: Section 187, which allows a "body corporate" that is a shareholder to authorise a person to represent it, who is then allowed to vote on a show of hands as well as ask questions.

On one occasion, bcIMC's custodian bank tried to request a poll at an AGM but met with various obstacles, including the fact that the company was not organised to hold one. The company then removed the resolution from the agenda.

➢ *For a copy of the bcIMC letters and detailed responses from the four Indian companies, please contact ACGA.*

The responses that bcIMC received to its request for a poll are similar to the responses ACGA receives when discussing this issue with Indian companies and regulators. Both tend to rely on the legal status quo as their defence and express surprise that investors are concerned about the way in which meetings are run or votes counted. A common response from companies is to say, as one manager did: "Institutional investors talk to us always outside the AGM, never within the AGM…I have never even seen our foreign institutional investors at our AGMs or their representatives."[9] Or as another advised: "If one of our foreign investors wants to have their votes counted, they should either send a staff member or a lawyer to the AGM, that way they do not have to worry about their proxies not being counted on a show of hands."[10]

As noted earlier, most global institutional investors face challenges attending AGMs in foreign countries, either for reasons of distance, the clustering of AGM dates, or because they invest in a very large number of companies. Annual shareholder meetings in many Asian, European and North American jurisdictions, for example, are typically held in the middle of the year, between May to August. Yet also for reasons given above,

attendance in person or by proxy at an AGM in India will not necessarily ensure that a poll will be called and votes properly counted.

Not publishing results

The lack of voting by poll in India translates into an absence of detailed information on the results of meetings.

Even if polls are called, the results are not always published on the company's website or those of the exchanges—because there is no legal requirement to do so. One of the few companies that has taken a poll and published the results in detail was state-owned Indian Oil in 2007 and again in 2008. It held a poll on four resolutions at its AGM in 2007 and published the total votes cast both for and against the following day (see table in Appendix 1). In 2008, it followed the same practice for just one resolution. The reason the company took a poll in 2007—and on only four resolutions—was because a poll was demanded by two individual shareholders who held sufficient shares. Interestingly, the votes were first passed on a show of hands before going to a poll.

The practice of what is published, if anything, tends to vary not only from company to company, but also from year to year, as the table below shows (covering the same large-caps as in the table on page 15). If a company publishes the minutes of its AGM one year, there is no guarantee that it will do so again the following year. Although some companies publish their minutes on the BSE or NSE websites, or provide a summary simply saying that all resolutions were passed, most companies do not. What is striking is how long it takes most companies to publish: some release their results within one day, but most take anything from a couple of weeks to a few months to publish an announcement.

Company	Latest AGM results published?	Year	Time lag (days)
Reliance Industries	Yes	2009	2
ONGC	Summary minutes	2009	0 on BSE; 28 days on NSE
Bharti Airtel	Summary minutes	2009	0 (same day)
NMDC	No	2009	--
Infosys Technologies	Transcript/webcast	2009	0 (same day on company website)
State Bank of India	No	2009	--
DLF	No	2009	--
Kotak Mahindra	Summary minutes	2009	13
Wipro	Summary minutes	2009	37

Source: ACGA research. *(See Appendix 1 for the background data from which this table was compiled.)*

A new company bill

Although discussions about amending the company law have been ongoing in the Indian Parliament and government for many years, the new Companies Bill, 2009 does not address many of the issues raised above. What it will do is allow for board meetings to be conducted via video conferencing, require special resolutions for a number of matters that are currently presented as ordinary resolutions (such as related- party transactions and appointing the managing director), and greater disclosure of related transactions and other matters. Yet it largely ignores the issue of shareholder meetings and voting.

The Bill reverts back to the Companies Act, 1956 on the question of giving proxies the right to vote a show of hands (and not just on a poll)[11]. Regulators, company executives and professionals give various explanations for this, including the allegation that shareholders could "hijack a meeting", while proxies could choose not to follow the instructions given by the shareholder appointing them (even if this did happen, it is likely to have only a minor impact on the outcome of a meeting, since the company's "promoter" or controlling shareholder would normally have a sufficient number of friendly shareholders in the meeting to ensure that any votes by hand were passed).

The new Bill also states that if a poll is called, the chairman can "appoint such number of persons, as he deems necessary"[12] to count the vote. However, there is no mention of the need for an independent scrutineer to audit the vote, as is the practice in other markets such as Hong Kong and China. Nor do any poll results have to be published.

The Ministry of Company Affairs resubmitted the Bill to Parliament on August 3, 2009 after national elections finished—renamed the Companies Bill, 2009—and the Parliament's Standing Committee on Finance should be reviewing the Bill shortly.

Recommendations

In order to improve the management and transparency of shareholder meetings in India, and to allow all shareholders (domestic and foreign) to participate fully in these meetings and make an informed vote, we recommend that companies implement the following measures (if they are not doing so already):

1.1 Ensure that the quality, transparency and reliability of the information in shareholder meeting agendas is sufficient to allow responsible investors to make informed voting decisions on each resolution.

1.2 Post the meeting notice (final agenda) and explanatory notes (detailed circular) for all general meetings, both annual and extraordinary, on the company website as well as on the websites of both the Bombay Stock Exchange (BSE) and the National Stock Exchange (NSE).

1.3 Ensure that the notices are easy to find (eg, they are prominently and separately displayed on the company website homepage and/or within its investor relations section). This would not preclude companies from including the notice as part of their annual report as well, if they wished to do so, but our recommendation is that this would not be the only means of dissemination.

1.4 Archive notices for the past 10 years on both the company website and on the BSE and NSE websites.

1.5 Release meeting notices and explanatory notes at least 28 days before annual general meetings (the current rule in India is 21 days). This will allow global institutional investors sufficient time to study the meeting agenda and make an informed vote. (Note: 28 days represents global best practice for the release of AGM agendas.)

1.6 Conduct voting on all resolutions at general meetings by a poll. Engage an independent scrutineer, such as a share registrar or law firm, to count the vote. (Note: If any vote is conducted by a show of hands, allow proxies to vote.)

1.7 Allow proxies to speak at meetings, irrespective of whether the company law is amended on this point. (Law and regulation sets a minimum standard, not necessarily the best practice that companies can follow.)

1.8 Publish full voting results on the company website and on the BSE and NSE websites within 24 hours of the meeting. ("Full" results means the total number of votes cast "for" and "against" on each resolution, and any abstentions.)

We also recommend that SEBI encourage the top 100 listed companies in India to start voting by poll as soon as possible.

It is worth emphasising that evidence from around Asia and other parts of the world shows that many of these reforms are relatively simple and cheap to implement. Recommendations 1.1 to 1.4 are largely good housekeeping matters and could be achieved with minimal additional cost to a listed company (although some negotiation with the stock exchanges may be required on Recommendation 1.3).

Recommendation 1.5 on voting by poll is usually seen by listed companies as something both costly and complicated (hence time consuming). The reality is that it is quite cheap (relative to the cost of holding an AGM) and technically much simpler than companies appreciate. Polls became the norm for large caps in Hong Kong before the listing rules were changed and they became mandatory in January 2009. They are also practiced by the largest listed firms (top 50 by market cap) in both China and Thailand, are the norm in the US, and are increasingly adopted in the Netherlands and the UK.

Recommendation 1.6 on allowing proxies to speak at meetings requires only a policy change on the part of the board of directors. Recommendation 1.7 on publishing full voting results is not hard to implement once all votes have been counted.

"Polls" vs "ballots"

For many companies, the term "voting by poll" conjures up the dreaded notion of "voting by ballot". A ballot refers to cases where votes on an individual resolution are counted, usually manually, in a meeting—a process that takes about half an hour. The assumption, therefore, is that counting the votes for all resolutions will take most of the day (since 10-12 resolutions x 30 minutes = 5-6 hours).

But this is not how polls are taken. One method involves collecting completed voting forms from shareholders at the end of the meeting, then closing the meeting, quickly counting the vote and announcing it later the same day or the following day. Another is more immediate—using electronic voting pads in the meeting. In both cases, the length of the AGM is not extended by taking a poll. It is an efficient process.

Issue 2: Related-Party Transactions

India has a weak regime governing related-party transactions. Regulation needs to be overhauled and minority shareholders accorded much greater protection

Due to the preponderance of family and state-controlled group companies in Asia, and the prevalence of both listed and unlisted entities under single families or groups, related-party transactions assume a greater significance in business and governance terms than they do in markets where listed companies lack large controlling shareholders and where the parent holding company is the primary listed vehicle.

In Asia, relationships between companies—parents and subsidiaries, listed and affiliated unlisted firms—can be opaque and will sometimes lead to transactions harmful to public shareholders. Under pressure from vested interests in the market and government, regulators often struggle to provide the right balance between protecting minority shareholders and allowing legitimate arms-length transactions between connected companies.

While India has laws and regulations governing related-party transactions, they provide weak safeguards for minority investors. Indeed, India's rules in this area are considerably less developed than many other Asian markets. Common features of related-party regulation in other markets include such things as:

- Drawing a distinction between one-off transactions (that may need to be regulated, especially if they are large) and continuing or recurring transactions of goods and services "in the normal course of business" (that probably do not need to be regulated, especially if they are small).
- Allowing exemptions for one-off transactions that are small and "non-material" to a company's business (ie, which fall below a certain percentage threshold).
- Mandating disclosure of transactions that are larger and more material (and which fall between certain percentage thresholds in terms of size).
- Requiring independent shareholder approval in an EGM of large transactions in which the controlling shareholder has an interest (and which are above a certain percentage threshold in terms of size).

Before discussing the India situation in detail, we briefly look at how Hong Kong and Singapore approach this issue.

The Hong Kong model

Within the region, Hong Kong has some of the most stringent rules on related-party transactions (called "connected transactions"). The rules are designed to "ensure that the interests of shareholders as a whole are taken into account by a listed issuer" when that issuer enters into a connected transaction; and to provide "certain safeguards against listed issuers' directors, chief executives or substantial shareholders (or their associates) from taking advantage of their positions".[13] (Chapter 14A, Listing Rules)

The Hong Kong Listing Rules contain a general requirement that companies should promptly disclose connected transactions to the market and subject them to independent shareholder approval (ie, those shareholders not linked to management or the controlling shareholder, or which have a material interest in the transaction).

To avoid over-regulation of trivial transactions, however, the Listing Rules allow "certain categories of transaction"[14] to be exempt from both the disclosure and independent shareholder approval requirements, while others only need to be disclosed.

Independent shareholder approval is generally reserved for the biggest and most material transactions, such as those that equal or exceed 2.5% of an issuer's total assets or revenue, or where the above percentage ratios are equal to or more than 25% and the purchase price is greater than HK$10 million.

Transactions smaller than those above are subject to disclosure requirements only. (Note: The disclosure rules are quite specific and cover both announcements and circulars.)

Meanwhile, very small transactions (such as those valued at less than 0.1% of an issuer's total assets or revenue) and various types of continuing transactions are wholly exempt from the disclosure and independent shareholder approval requirements.

The Hong Kong rules also contain other safeguards, including:

- Where transactions are subject to independent shareholder approval, a company must form an "independent board committee" (comprising only independent directors) to advise shareholders whether the transaction is fair and reasonable.
- In such cases, the issuer must also appoint an independent financial adviser to make recommendations to the independent board committee and shareholders.
- The Stock Exchange will "aggregate a series of connected transactions and treat them as if they were one transaction" if they are all completed within 12 months or are related. This stops listed companies from splitting up one large transaction into several and thereby getting around the rules.

The Singapore model

In Singapore, the Listing Manual states that the rules on "interested person transactions" are designed to prevent a company's director, chief executive or controlling shareholder (or their associates) from influencing the company, its subsidiaries or its associated companies from entering into transactions that would "adversely affect the interests of the company or its shareholders".[15] (Chapter 9, Listing Manual)

As in Hong Kong, companies in Singapore are required to disclose such transactions and obtain independent shareholder approval for any interested person transaction of a value equal to, or more than:

- 5% of the group's latest audited net tangible assets; or
- 5% of the group's latest audited net tangible assets, when aggregated with other transactions entered into with the same interested person during the same financial year.[16]

The above rule does not apply to any transaction below S$100,000 (US$71,000).

The situation in India
Compared to Hong Kong and Singapore, India's rules on related-party transactions are sparse. They contain no requirement for independent shareholder approval of significant transactions, nor much in the way of disclosure and reporting rules.

India's regulations are found in three main documents: the Companies Act, 1956; Clause 49 of the Listing Agreement; and Accounting Standard (AS) 18. A summary of key provisions follows:

Companies Act

The Companies Act has four main sections that concern related-party transactions.

- **Section 295** deals with loans to directors and, in essence, states that companies may not make loans to their directors (or directors of their holding company), or any partners or relatives of any of their directors, or any firms in which any of their directors (or relatives of a director) is a partner, and so on, *without* first obtaining the "previous approval of the Central Government". (Note: Exemptions are provided for private companies that are not subsidiaries of public companies, banks, and holding companies making or guaranteeing loans to subsidiaries.)

- **Section 297** requires directors to seek board consent for contracts with the company in which they or a relative are interested.

- **Section 299** states that directors must disclose at a meeting of the board any direct or indirect interests in existing or proposed contracts or arrangements entered into by the company.

- **Section 300** bars directors from voting on, or participating in any board discussions regarding, any contract or arrangement in which they are directly or indirectly interested. (Note: Exemptions are provided for private companies that are not subsidiaries or holding companies of public companies. More interestingly, the Central Government can override this clause in favour of individual companies if it feels that it would "not be in the public interest to apply all or any of the prohibitions" in this section—for example, if it wanted to promote any industry, business or trade.)

While it is significant that the Companies Act places heavier obligations on public companies in this area, it is also worth noting that the penalties for non-compliance are, for the most part, minimal. With the exception of loans to directors—for which one of the sanctions is up to six months in prison—the penalty for contravening the law is a mere Rs5,000 (US$100 approx).

Clause 49

Clause 49 was issued in February 2000 by the Securities and Exchange Board of India (SEBI) and is the key section of the Listing Agreement that regulates the corporate governance of listed companies.

Clause 49 makes a number of references to related-party transactions, but all of them are brief and quite general. These include provisions stating that:

- Audit committees shall review annual financial statements (before submission to the board for approval) with particular reference to several factors, one of which is "disclosure of any related-party transactions" (sic).
- Audit committees shall also review, on a more general basis, any statements of "significant related-party transactions (as defined by the audit committee) submitted by management".
- Listed companies must periodically give their audit committees a summary statement of "transactions with related parties in the ordinary course of business", as well as details of "material individual (related) transactions" that are "not in the normal course of business" or not done on an arm's length basis ("together with Management's justification for the same").

Clause 49 also requires listed companies to submit a quarterly "compliance report on corporate governance" to the stock exchanges. One element of this is disclosure of the "basis of related-party transactions". Companies must also include a section on corporate governance in their annuals report and it is suggested that they include "disclosures on materially significant related-party transactions that may have potential conflict with the interests of the company at large".

Accounting Standard 18

AS 18 mandates that companies report related party relationships and transactions between themselves and related parties. While it largely follows International Accounting Standard (IAS) 24 on "Related Party Disclosures", there are important differences between the two standards. AS 18 does not require reporting related-party relationships or transactions between state-controlled enterprises. Nor does it require disclosure of the basis of pricing of such transactions, except in limited circumstances such as when a major asset is transferred to a related party at a markedly different price from the commercial price.

AS 18 also differs from IAS 24 in that disclosures have to made in the separate financial statements of a parent and its subsidiaries, if AS 18 applies to them, as well as in the consolidated financial statements. IAS 24, on the other hand, does not require wholly-owned subsidiaries to issue separate financial statements if its parent is incorporated in the same country and issues consolidated financial statements in that country.

Weak investor protection

As noted, what is most obviously lacking in India's rules on related-party transactions is any provision for independent shareholders to vote on major related transactions and detailed rules on disclosure.

It is not surprising that the Companies Act does not provide this, since company law has to cover all types of incorporated companies (listed and unlisted) and it is generally more efficient to deal with this issue through either securities law or listing rules. It is somewhat unusual, however, that the Companies Act gives the Central Government the power to approve loans to directors of state-owned companies, but does not accord the same powers to their shareholders. This could be interpreted as suggesting that the government thinks investors are not capable of making informed decisions. But what information would the government be privy to that shareholders should not have?

What is more surprising is that Clause 49's provisions are so general in nature and only seek to regulate related transactions through review by audit committees and disclosure in company reports (rather than prompt disclosure to the market through company announcements and circulars). Moreover, the recommendation that companies disclose "materially significant" transactions that may have "potential conflict with the interests of the company at large" implies that such transactions are acceptable as long as they are disclosed.

It should also be pointed out that no other section of the Listing Agreement deals with related transactions. In contrast, Hong Kong's equivalent rules run to 42 pages (Chapter 14A of the Listing Rules), while Singapore's comprise 11 pages (Chapter 9 of the Listing Manual).

Nor does the SEBI Act have much to say on related transactions. This Act established SEBI in 1992 and covers the powers and functions of the board, such as protecting the interests of investors in securities, promoting the development of the market, and regulating such matters as fraudulent and unfair trade practices and insider trading. While there are separate guidelines under the Act for insider trading, for example, the same does not apply to related-party transactions.

When asked about this situation in April 2009, SEBI told ACGA that the regulation of related-party transactions in India was more the purview of the Ministry of Corporate Affairs (MCA) rather than itself. However, as noted above, regulating the related transactions of listed companies through a general company law is not necessarily the most efficient way to address this issue.

SEBI only recently published regulations in the Issue of Capital and Disclosure Requirements, 2009, which replaced the Disclosure and Investor Protection Guidelines, 2000. Whereas the earlier regulations made scant reference to related-party transactions (other than the fact that promoters/controlling shareholders should disclose them in their financial reports), the new regulations do devote a paragraph on how related-party transactions should be disclosed according to Accounting Standard 18.

Negative market impact
The lack of effective rules in this area has led to negative consequences for investors in India. According to domestic Indian fund managers, typical transactions that listed companies engage in include:

- Spinning off valuable assets from listed companies to unlisted private entities for the benefit of promoters.
- Spinning off investments in group companies to a holding company, valuing the investments at a large discount to fair value, then buying back the shares of the holding company from the market.
- Shifting new business to unlisted private entities and letting an affiliated listed company pay for branding and distribution costs.

The following case study highlights one type of problem (the company name has been disguised): In 2009, the board of Company B, which is part of a large foreign conglomerate, approved the sale of its equity stake in a wholly-owned subsidiary, Company C, to its parent company overseas. The foreign parent owns more than half of Company B.

The market questioned the valuation of Company C, which seemed to be on the low side compared with other companies in the same sector, and wondered why its profitability had declined for the three quarters prior to the sell-off. In the year ending September 2008 its profit before tax was less than half that in the same period the year before, yet revenue had remained fairly steady. Moreover, Company C continued to be one of Company B's best performing subsidiaries, if not its most profitable.

Some investors believe the exercise was an attempt by Company B to depict a dismal financial performance to justify a lower valuation. If Company B had sold the subsidiary by open bidding, it would probably have received a higher price, thereby benefiting all its shareholders. Despite the material nature of this related transaction, the sale was never brought to independent shareholders for approval.

It was the Satyam Computer case in late 2008, however, that most seriously exposed the weaknesses of related-party regulation in India. Incredibly, the plan of the company's controlling shareholder and chairman, Ramalinga Raju, to spend most of Satyam's reported cash reserves to acquire control of two companies run by his sons—and in an unrelated sector, property—only required the approval of Satyam's board of directors. The purported facts were as follows:

- The purchase price for the two companies, Maytas Properties and Maytas Infrastructure, was US$1.6 billion—which would have depleted Satyam's reported US$1.1 billion surplus cash reserves at the time.
- Raju claimed that the valuation for the acquisitions had been done by one of the Big 4 global audit firms, but refused to name it. There followed a public denial by each of the firms of having carried out the valuation work.
- An independent director, Mangalam Srinivasan, resigned from Satyam on December 25, 2008, stating that she had voiced reservations about the transaction during the board meeting, but had failed to cast a dissenting vote or ensure that her views were put on the record. This nevertheless gave the lie to the company's claim that the board had unanimously approved the deal.

- It transpired that the compensation package of one of the independent directors was more than seven times that of the other independent directors and well above the market rate. It turned out that he was carrying out consulting work for the company—something that should have barred him from being an independent director.
- Raju remained in the board meeting throughout the discussion on Maytas, despite having a clear conflict of interest.

Even though Raju later admitted that he had been defrauding the company for a number of years, leading him to propose the purchase of the two companies, this does not detract from the fact that transactions of such magnitude—and which posed such clear conflicts of interest for the controlling shareholder—do not require independent shareholder approval in India.

Objections
Various counter arguments are made in India against introducing stronger rules on related-party transactions. One is that allowing shareholders to vote on such transactions would interfere with the smooth operation of companies. Another is that since many promoters (ie, controlling shareholders) have more than 50% of the voting rights in the company, the result of any vote would be a foregone conclusion.

These objections miss the point: as rules in other markets show, related-party regulation does not require every single transaction to be voted on—only the largest and most material. Moreover, the second objection is not relevant, since connected shareholders would not be permitted to vote in a meeting of independent shareholders.

Recommendations
We believe that certain reforms would enhance the governance of related-party transactions in India and strengthen investor confidence in the country's capital markets. We recommend that the government and regulators:

2.1 Introduce comprehensive regulation of related-party transactions, including giving independent shareholders the powers to approve large transactions above a certain limit and enhancing disclosure requirements on other material transactions. Such regulation could be provided for in both the Listing Agreement and new SEBI regulations or guidelines.

2.2 Require the appointment of an independent financial advisor and an independent board committee to determine whether material transactions are fair and reasonable to all shareholders.

2.3 Require independent directors to exercise their duties more diligently and protect the interests of minority shareholders, especially in cases where the majority shareholder is also the manager of the company. Some degree of legal liability could be considered for directors in cases such as Satyam.

2.4 Encourage listed companies with numerous related transactions to set up a related-party transaction committee of their board. This would scrutinise such transactions, recommend to the board if shareholder approval should be sought, advise on disclosure and judge the fairness of transactions.

OECD Guide on Abusive Related Transactions

In September 2009, the OECD published a booklet titled "Guide on Fighting Abusive Related Party Transactions in Asia". It is a product of a task force set up under the OECD Asian Roundtable on Corporate Governance and provides a useful overview of the nature, definition and regulation of related-party transactions in Asia, as well as recommendations on how to develop a regime for regulating such transactions.

One section of the guide deals with legislative and regulatory approaches to controlling related transactions and mentions Hong Kong, Singapore, Malaysia and China as jurisdictions offering useful guidance. There is, not surprisingly, little mention of India.

CFA Institute report

In January 2009, the Asia-Pacific office of the CFA (Chartered Financial Analyst) Institute Centre for Financial Market Integrity published its report "*Related-Party Transactions: Cautionary Tales for Investors in Asia*".

The report discussed the "prevalence" of related-party transactions in Asia and how they affected the interests of minority shareholders. Focussing on three jurisdictions—China, Hong Kong and South Korea—the report concentrated on three main issues:

- Identifying ways in which such transactions had disenfranchised minority shareholders;
- Exploring how effectively prevailing systems of checks and balances had protected such investors; and
- How these systems could be improved.

Some of the conclusions in the report regarding better investor protection from the risks of related party transactions included:

- Investors in Asian companies should engage more with controlling shareholders, encouraging minority or independent shareholders to stop voting with their feet and instead "exhaust all available avenues for expressing their views";
- Related-party transactions should pass effective approval and disclosure processes. Regulators that had not already done so, the report stated, should define material related-party transactions and the threshold values after which the transactions must be disclosed or subject to approval procedures. It stated that thresholds should not be so high as to allow controlling shareholders to conduct a series of small deals with ultimately the same effect as a single large transaction, nor so low as to be costly and cumbersome to administer;
- Corporate boards should include more independent directors;
- Asian companies should adopt greater transparency on related-party transactions. The report suggesting that as a best practice, companies should adopt and disclose a statement on policy on such transactions, formalizing the review process with a level of detail above and beyond what had been stipulated by the regulators; and
- Regulations on these transactions should be backed by law, such as by giving listing rules statutory backing, with appropriate civil penalties and orders of compensation in case of a breach.

Issue 3: Preferential Warrants

The scope for the misuse and abuse of warrants in India is considerable. Regulation of their issuance to promoters needs to be tightened

The use of warrants as a fund-raising tool is markedly different in India to other major markets in Asia or developed countries. In most markets where warrants are offered, they typically act as a sweetener accompanying a rights issue or a new issue of bonds or preferred stock. They allow the holder to buy a "proportionate amount of stock at some specified future date at a specified price, usually one higher than the current market price".[17] They are "generally issued as an incentive to investors to accept bonds or preferred stocks that will be paying a lower rate of interest or dividends than would otherwise be paid".[18] Warrants are like call options, but have longer life spans—sometimes of several years.[19]

In India, however, warrants rarely form part of a larger issuance of securities to a company's shareholders. They are normally offered instead to the promoters (controlling shareholders) of the company and on a preferential and discounted basis. While the ostensible reason for issuing warrants is to raise capital for companies, the practical effect is that promoters are able to increase their level of shareholding at a discount to the market price. This not only dilutes other shareholders, but contradicts a basic principle of company law in developed markets that insiders should not be allowed to sell stock to themselves at a discount (unless it forms part of a general rights issue, for example, to all shareholders or an approved stock option plan for management).

Both the listing rules of the Singapore Exchange (SGX) and the Stock Exchange of Hong Kong (SEHK) allow warrants to be issued for cash "other than by way of a rights issue"[20], but they do not permit such products to be sold purely to controlling shareholders. The SGX listing rules state that an issue must not be placed to the company's directors and substantial shareholders, immediate family members of the latter, related companies, and corporations where the company's directors or substantial shareholders have an aggregate interest of at least 10%.[21] The SEHK rules state that, unless independent shareholders' approval has been obtained, the issue of securities to a connected person under a "general mandate" (ie, private placement) is only permitted in certain limited circumstances: where the connected person receives a pro-rata entitlement of securities issued to all shareholders; the securities are part of a share option scheme; or where the connected person is acting as an underwriter of an issue.[22] (emphasis added)

Similar constraints and principles do not exist in India. There are rules governing private placements—namely the SEBI (Disclosure & Investor Protection Guidelines) 2000 and the Companies Act, 1956—but both contain loopholes regarding preferential share issuances. These loopholes have been replicated in SEBI's new regulations on the "Issue of Capital and Disclosure Requirements", which took effect in September 2009 and replaced its Disclosure Guidelines of 2000. In a press release, SEBI stated that the Regulations were "primarily" a "conversion" of the 2000 Guidelines, but with "certain changes" such as removing redundant provisions and modifying certain provisions. The new Regulations state that a company may "make a preferential issue of specified securities" if:

- It has been passed by its shareholders in a general meeting;
- All the equity shares, if any, held by the proposed allottees in the issuer are in dematerialised[23] form;
- The issuer is in compliance with the conditions for the continuous listing of equity shares, as specified in the Listing Agreement;
- The issuer has obtained the Permanent Account Number of the proposed allottees.

The only check and balance in the rules above is the first measure requiring shareholder approval of the preferential securities and a 75% vote in favour. While this hurdle sounds reasonably high, in practice it is not: all shareholders may vote on the resolution, including promoters, and the latter typically own large or majority stakes in the company; hence approval is usually a foregone conclusion. Neither the Companies Act nor the Listing Agreement in India state that only independent shareholders without a conflict of interest should be permitted to vote—a standard feature of related-party or connected transaction regulation in other markets. Moreover, the vote in India is almost always counted by a show of hands, thus making approval even easier (since this system of voting disenfranchises institutional investors who are more likely to vote against).

A flawed pricing model

The formula for the pricing of warrants can also give rise to abuse. The pricing model allows promoters to issue preferential warrants to themselves at effective discounts, because the Regulations provide a fixed formula for pricing warrants at historic prices. The price should not be less than the higher of the following:

- The average of the weekly high and low closing prices of the related equity shares quoted on the recognized stock exchange during the six months preceding the "relevant date"[24]; or
- The average of the weekly high and low of the closing prices of the related equity shares quoted on a recognized stock exchange during the two weeks preceding the relevant date.

According to an Indian research analyst based in Mumbai**,** the model gives rise to abuse because it allows promoters to set the conversion price of warrants at a level below the market price of shares (in a rising market), thus allowing them to buy the warrants at an effective discount and lock in significant potential profit. The return is also enhanced because warrants in India have a relatively long life span of 18 months.

An Indian lawyer explained that the main problem with the pricing formula above is the definition of "relevant date". For a preferential issue of convertible securities, such as warrants, the relevant date is defined as being either the date 30 days prior to the date of the shareholder meeting held to approve the issue or 30 days prior to the date on which the holders of the convertible securities become entitled to apply for the equity shares. Such choices open the door to potential promoter misconduct (since promoters will clearly have inside information about the prospects for their company).

The table on the next page shows the potential dilution for existing shareholders in terms of value and percentage of market cap in a number of companies that issued warrants in early 2009 or converted warrants issued previously. These names were provided by an

ACGA institutional investor member with long experience of the Indian market. The details of the warrants were plugged into an Excel file created by Credit Suisse to calculate possible dilution levels.

Company	Shriram Transport	Bajaj Holding and Investment	Anant Raj Industries	Unitech	Bajaj Hindusthan	Reliance Infra-structure	Aditya Birla
Bloomberg code	SHTF	BJHI	ARCP	UT	BJH	RELI	ABNL
Warrant conversion price (Rs)	290	449.58	87	50.75	52.1	1,000	540.54
Expiration period (months)	18	18	18	18	18	18	18
Number of warrants issued (millions)	8	10.11	20	227.5	14.5	42.9	18.5
Date of issuance of the warrants	12-Dec-07	16-Jul-09	25-Jun-09	19-May-09	14-May-09	22-May-09	18-May-09
Standard Deviation (volatility of share price)	75%	75%	80%	70%	86.9%	70%	60%
Potential dilution for existing shareholders ($ m)	22	12	10	113	17	218	55
Potential dilution for existing shareholder as % of market cap	1.36%	1.41%	1.79%	3.8%	5.2%	4.3%	4.4%

Source: Model provided by Credit Suisse

Boilerplate disclosure

The new 2009 Regulations, like the earlier Guidelines, state that companies planning to issue preferential securities must provide an explanatory statement to shareholders outlining the purpose of the issue; the intention of promoters, directors and key managers to subscribe to the offer; the shareholding pattern of the company before and after the issue; the time frame within which the preferential issue shall be completed; the identity of the proposed allottees; whether there will be a change of control, and so on. But a review of the meeting notices of some companies indicates that the language used is often boilerplate, giving minimal information to investors.

For example, Anant Raj Industries, a construction and infrastructure developer, released an EGM notice on May 29, 2009 seeking approval from shareholders to issue 20 million warrants to the promoter group, Anant Raj Meadows Private Ltd. The notice stated that the object of the issue was to "meet the working capital requirements for the existing

operations and for the expansion of the company's business operations which include further investments in projects relating to hospitality sector, development of infrastructure for the information technology sector, developing Special Economic Zones and service apartments". Following the warrants issue, the promoters and promoter group shareholding in the company would increase from 64.59% to 66.95%.

In another example, Unitech, a property developer, stated in a May 18, 2009 notice to shareholders that the company required the funds in the "near future for business expansion, enhancement of competitiveness, repayment of loans and strengthening of its financial position through long-term resources".

Where are the regulators?
Despite the damage that preferential warrants can clearly do to minority shareholder interests, not to mention the reputation of India's capital markets, financial regulators have been slow to act on this issue. The problem has been brought to their attention on a number of occasions, most recently through a court case that was referred back to SEBI by the Bombay High Court on June 18, 2009.

The case was brought by a Mumbai-based shareholder association, Rajkot Saher Jilla Grahak Suraksha Mandal, founded by former MP Ramjibhai Mavani, against the Union of India. According to the petitioner, the case was brought to court in order to:

> "expose a massive and orchestrated scam by the promoters and people enjoying controlling interest in a large number of companies, in exercising the powers under Section 81 (1A) of the Companies Act, 1956… read with the Securities and Exchange Board of India (Disclosure & Investor Protection) Guidelines 2000…., arbitrarily for their personal aggrandizement at the cost of the company and its investors".

The petition went on to state:

> "that the uniformity in the actions of the promoters indulging in exercising the powers under Section 81 (1A) of Act and the blatant and flagrant misuse of the guidelines under Chapter XIII of the Guidelines, was a very disturbing aspect demonstrating the inadequacies in the Guidelines for Preferential Issues contained in Chapter XIII of the Guidelines, which was being misused by the promoters controlling the companies, by exercising the discretion to issue further share capital solely for their personal ends, to the exclusion of the shareholders by taking undue advantage of the absence of sufficient safeguards/deterrents…"

The petition asked that SEBI alter the Guidelines to:

- Protect the interest of investors;
- Further issue of share capital must be for the benefit of the company as a whole;
- Further issue of share capital ought not be used as a tool for the personal aggrandizement of the people vested with the discretion to decide the further issuance of share capital; and
- To ensure that there are sufficient safeguards/deterrents against the misuse of the above power/provision.

Rajkot Saher cited a number of companies, such as Aditya Birla Nuvo Ltd, Tata Power Ltd, Reliance Infrastructure Ltd, Pantaloon Retail Ltd and Hindalco, as having cancelled the promoters' warrants, forfeiting the upfront money paid by the promoters, and again reissuing the warrants at a lower price. It stated that the board of directors of these companies had "misled" SEBI, the Stock Exchanges and the shareholders regarding the requirement of funds for the company at the initial preferential allotment of warrants to the promoters.

A key question the Association raised was that, if the company needed the funds, why did the board cancel the warrants or allow the warrants to lapse, and in some cases reissue the same number of warrants to the same group of promoters at a lower price, thereby raising lower amounts of equity? A whole-time member of SEBI, Dr. K. M. Abraham, who oversaw the case, essentially concluded that the current regulations provided enough checks and balances for shareholders and prevented promoters from abusing the Guidelines (now superseded by the Regulations).

Jayant Thakur, a Mumbai-based chartered accountant, wrote an article on July 31, 2009, the day following the ruling, titled "Issue of Banning Share Warrants to Promoters – SEBI order". Thakur criticised SEBI's stance that the company and its shareholders were benefiting from forfeiture of upfront payments. He argued that "effectively a significant portion [of the upfront payment'] goes back to the promoters to the extent of their holding in the company".

On a more positive note, however, Dr. Abraham said that as regards the request by Rajkot Saher that SEBI should "immediately issue regulations prohibiting the promoters from voting in the general meeting on any resolution in which they are interested in", the regulator should "take note" and begin a "consultative process including taking views of market participants and various other stakeholders, to suggest policy changes, if required".

Recommendations

We believe that certain reforms are needed to control the issuance of preferential securities in India and fundamentally strengthen investor protection. We recommend that:

3.1 The issuance of preferential shares, warrants or other securities to promoters and other connected persons be prohibited (as in other markets), except under the limited circumstances envisaged in markets such as Hong Kong (ie, where the securities are part of a pro-rata entitlement made available to all shareholders on an equal basis, or as part of a shareholder-approved stock option scheme).

3.2 Companies be required to seek shareholder approval at their annual general meetings for the issuance, over the subsequent 12 months, of any new shares at a discount to a limited group of (non-controlling) shareholders. Strict rules should govern the size and discount of such offerings.

3.3 Listed companies review the way they use warrants and limit their application to forming part of a wider issue of debt or equity securities (ie, where warrants act as sweeteners for investors).

Insider trading?
The fact that promoters of listed companies are selling preferential securities to themselves raises the issue of potential insider trading.

In a recent article[25], Shuva Mandal, a lawyer at AZB Partners in Mumbai, wrote that "in many ways, almost all warrant issuances by Indian listed companies to their promoters, envisage clever leverage structures being worked out by the promoters". He described two scenarios whereby promoters gain through inside information: A promoter, knowing that his company, A Ltd, is set to benefit in the future, subscribes to 100 warrants that entitle him to 100 equity shares at Rs20 per share, as per the minimum pricing formula set out in the SEBI Regulations. Under these circumstances, the promoter will pay Rs5 per share (25% of Rs20) for a total of Rs500. At the end of 18 months, when the warrants come due, the scenario could unfold in two ways, according to Mandal:

Equity shares of A Ltd trading at Rs30
The promoter could pay the balance of Rs1,500 by taking out a loan and become the owner of 100 equity shares, which at the current market price would be worth Rs3,000 (and for which he paid only Rs2,000). According to Mandal, the promoter could theoretically sell 50 existing equity shares—since the equity shares arising from the warrants would be locked—and pay back the loan the following day. Hence, for a price of Rs500, the promoter would be able to increase his stake by 50 shares.

Equity shares of A Ltd trading at Rs 10
The promoter would lapse the warrant, forgoing the Rs500 option price he had paid earlier. The company would then lose the additional funds that it had earlier stated it needed to pursue its business goals. As Mandal argued further, if fund raising was the primary objective of the warrant issue, how could a board of directors allot fresh warrants at a lower price to the same set of promoters at the same meeting in which the decision was taken to lapse the first set of more expensive warrants? This is a practice that a number of companies have indulged in.

Issue 4: Corporate Disclosure

The scope, depth, timeliness, consistency and formatting of corporate financial disclosure in India could be greatly improved

While leading blue-chip companies in India have a well-deserved reputation for the excellence of their financial reports, across the market the quality of corporate disclosure is mixed. The issue is not a shortage of rules—listed companies must comply with numerous standards laid down in the Companies Act, SEBI regulations, and the Listing Agreement of the stock exchanges. Rather, it is that disclosure is often insufficient, rules are sometimes inconsistent, the format of financial reports can vary from company to company (even within the same group), and access to company reports online is more difficult than one would expect.

During 2009, SEBI made progress on a number of fronts. In early February, it required companies for the first time to provide details of any shares pledged by promoters as well as a quarterly statement of the share ownership patterns of promoter groups (previously companies only had to disclose the latter once a year). This rule change followed the Satyam scandal where the chairman had pledged his shares in return for loans from various non-bank financial institutions.

In September 2009, SEBI released a discussion paper on proposals relating to disclosure and accounting. Its Standing Committee on Disclosures and Accounting Standards (SCODA) reviewed seven issues proposed by the SEBI Board, including a requirement for professional qualifications for CFOs, the rotation of audit firms or partners, and the interim disclosure of balance sheets. In November 2009, the SEBI Board accepted some of the recommendations from the Committee, including a suggestion for mandatory publication of half yearly balance sheets. Further decisions and details are expected soon. (See below for further discussion of this paper.)

Despite these regulatory and policy developments, however, the core problems outlined above with corporate disclosure remain.

Disclosure limitations

Investors in India often express frustration at the quality and consistency of financial information provided by many companies. While annual reports are generally quite good in terms of content, publication can be slow (sometimes up to six months after year-end). This means investors are often waiting a long time for audited annual results. Prior to this, only unaudited quarterly results are available from most companies.[26]

Quarterly reports provide limited information—most contain only basic P&L numbers, with no accompanying balance sheet or cashflow statement. There can be discrepancies in the numbers from one period to the next, some companies change their accounting policies to produce more favourable results, and quarterly financials are often not consolidated. Balance sheets, meanwhile, only need to be published once a year (although this should soon change to twice a year, as noted above).

The limited nature of information provided in quarterly reports can be seen from a comparison of the report of a major Indian telecoms company with that of a comparable company in the US. One big difference is that the Indian company provides much less

detail in its P&L statement on sources of revenues—there is no segmented sales data. While the data may appear in other parts of the report, this can change from year to year because providing such information is not a requirement under Clause 41 of the Listing Agreement. Titled "Preparation and Submission of Financial Results", this clause provides a format for companies to follow in submitting quarterly financial results (see Appendix 3 for details).

While the Indian firm provides more information on expenses than revenues—as is required by Clause 41—it does not include depreciation/amortization in its operating expenses (as it should under the rules). Instead, it produces an "EBITDA" figure, after which it deducts finance charges, depreciation/amortization and so on. The US firm produces an "operating income" figure that does include depreciation and amortization.

It is in the area of the balance sheet, however, that the differences are most apparent. While the Indian firm should be commended for producing a balance sheet (since this has not been required to date under Clause 41), the level of detail provided is considerably less than the US firm and the formatting of figures is a little odd. As the table on the next page shows:

- The Indian firm does not include a "cash and cash equivalents" figure under current assets. Instead, the company's cash level has to be interpreted from a "net debt" figure under liabilities (ie, total debt less cash = net debt).
- While the US firm produces estimates for intangible assets under assets, the Indian firm does not.
- Information on current liabilities is noticeably less detailed in the Indian balance sheet than in the US one.
- The US balance sheet provides more clarity on short and long-term debt.

While some of these disclosure and formatting problems can be resolved by investors recalibrating the numbers in P&L statements and balance sheets, this is not the case when detailed figures are not provided—or not provided until several months later in the audited annual accounts. As one investor said of some bank financial reports in India, "sometimes we cannot easily decipher the net interest income, because the interest income and the interest expense are lumped in with other items". Nor is it the case when, as another investor said, a company's financial position is artificially inflated by misrepresentation of liabilities on a fourth-quarter balance sheet. Such a "mistake" will only be rectified and made known to shareholders when the company's audited annual results are published.

(continued over)

Indian Company	US Company
Assets	**Assets**
Current assets: inventories, debtors, other current assets, and loans and advances. - (Does not include cash and cash equivalents)	**Current assets:** cash and cash equivalents; accounts receivable; prepaid expenses; deferred income taxes; and other current assets.
Fixed assets: gross block less depreciation providing the net block, and capital work-in-progress. Investments were a separate line item.	**Property, plant and equipment** (net) Goodwill; licenses; customer lists and relationships (net); other intangible assets (net); investments in equity affiliates; and other assets.
Liabilities and stockholders' equity	**Liabilities and stockholders' equity**
Strangely, the Indian company put its **stockholders equity** first, followed by liabilities	**Liabilities:** **Current liabilities:** debt maturing within one year; accounts payable with accrued liabilities; advance billing and customer deposits; accrued taxes; and dividends payable.
Current liabilities and provisions: only two line items -- current liabilities and provisions.	**Long-term debt**
Debt: secured loans (foreign currency loans and rupee loans), and unsecured loans (foreign currency loans and rupee loans). Then cash and cash equivalents were subtracted from the debt figure to produce a net debt figure.	**Deferred Credits and Non-current Liabilities:** deferred income taxes; post-employment benefit obligation; and other non-current liabilities.
	Stockholders' equity: common shares issued; capital in excess of par value; retained earnings; treasury shares (at cost); accumulated other comprehensive loss; and non-controlling interest.

Rule inconsistency

Underlying these issues is the fact that Clause 41 can be somewhat confusing. It states that quarterly results should be prepared "in accordance with the recognition and measurement principles laid down in Accounting Standard 25", issued by the Institute of Chartered Accountants of India (ICAI). In addition to the statement of income and expenditure, the ICAI standard requires that balance sheets be provided in interim results. Yet, as noted above, Clause 41 contains no such requirement and most listed companies—some of the larger ones excepted—only produce a balance sheet once a year in their annual report. As one investor pointed out, if any significant changes occur, such as capital raisings, investors might only know about them at the end of the financial year. He also said that even Indonesia, which always ranks below India in corporate governance surveys, produces better pro-forma balance sheets than India.

Online fragmentation

Accessing financial reports online can be difficult in India—and much more so than one would expect from a country with a strong reputation in IT. This is partly because Indian companies need to file different disclosure documents—or sometimes the same ones—with different regulatory bodies. There is no single central database from which all company reports, announcements, circulars and other documents can be accessed. It is also because the websites of listed companies are often poorly designed, slow and lack sufficient archived information.

In 2002, SEBI initiated the "electronic data and information filing and retrieval system" (EDIFAR), closely modelled on the SEC's EDGAR* system in the US. Launched with the National Informatics Centre, EDIFAR was to have been implemented in a phased manner, with 200 companies in the BSE Sensex, S&P CNX Nifty and BSE-200 indices filing financial reports, corporate governance reports, shareholding pattern statement and regulatory actions taken against the company. By the end of 2003, another 2,345 companies were to have filed with EDIFAR and, it was hoped, physical filing would eventually end for all actively traded companies on the exchanges. But EDIFAR failed to live up to its promise. While some companies are up to date, others seem to have stopped filing in 2005 or 2006.

A second initiative, the "corporate filing and dissemination system" (CorpFiling) took up the challenge in 2007. It was initiated by the National Stock Exchange and the Bombay Stock Exchange (BSE). While only 100 companies are mandated to file through this site, the portal states that its aim is to provide "a single interface to the investors to keep track of the latest filings of all the listed companies in India irrespective of the Stock Exchange". In fact, one can already find all of the disclosure announcements on the websites of the exchanges on CorpFiling. Unlike EDIFAR, however, the site is not as well-organised (see table below), making it more difficult to locate particular documents easily and quickly. Indeed, the portal is often very slow and frustrating to use. Nor does CorpFiling provide any information on action taken against companies by regulators.

CorpFiling	EDIFAR
Structure: 1. Announcements 2. Results 3. Shareholding pattern 4. SAST (Substantial Acquisition of Shares and Takeovers) 5. Insider trading	**Structure:** 1. Quarterly financial statements 2. Annual financial statements 3. Shareholding patterns 4. Segment results 5. Actions taken against company 6. Cashflow statement 7. Profit and loss account 8. Corporate governance report 9. Balance sheet 10. Annual report 11. ESOP

* Electronic Data Gathering, Analysis, and Retrieval.

Not only is accessing information online quite difficult at times, but the quality of company announcements is often inconsistent and poor. As noted in Issue 1 on "Shareholder Meetings and Voting", it is rare to find detailed announcements of AGM results on the websites of either the exchanges or companies. And even when a company does provide a full notice, it may not do so again the following year (as in the case of Bharti Airtel).

A further issue is that the online archiving of company reports and announcements is not as extensive in India as in some other regional markets. Whereas the BSE generally archives material for eight years and the NSE for five years, the Stock Exchange of Hong Kong has a database going back more than 10 years to 1999.

SEBI policy reform

The Satyam scandal was the catalyst for some new thinking on corporate disclosure and accountability in India. As noted above, SEBI published a discussion paper on September 14, 2009 on proposals relating to disclosure and accounting amendments in the Listing Agreement. The paper reflected earlier discussions in SEBI's Standing Committee on Disclosures and Accounting Standards (SCODA) with regard to seven issues[*] (and sought public comment on them):

1. Professional qualifications and financial literacy of CEOs and CFOs
2. Rotation of audit firms and/or partners
3. Appointment of an external audit firm to carry out internal audit
4. Modification of the external auditor's report in relation to enhanced disclosure of promoter shareholdings
5. Voluntary adoption of IFRS by listed companies with subsidiaries
6. Interim (half yearly) disclosure of balance sheets
7. Revised timelines for the submission of financial results

On November 9, 2009, the SEBI Board announced that it would amend the Listing Agreement in relation to three of these issues, namely:

- Allowing the voluntary adoption of IFRS by listed entities with subsidiaries;
- Requiring half yearly disclosure of balance sheets (which must provide audited figures, or non-audited figures with limited review); and
- Approving some of the new deadlines recommended by SCODA for the submission of financial results. (Namely, a more flexible requirement for the disclosure of quarterly results—45 days after the period end rather than the current 30 days—but a tighter deadline for the disclosure of audited annual results by companies that opt to produce "stand-alone" (ie, unconsolidated) annual results instead of an unaudited fourth quarter report—reduced from 90 days to 60 days.)

It is not clear, however, when these listing rule changes will take effect. Moreover, the changes to the disclosure deadlines still fail to address the problem of when a company

[*] Note: The wording of these issues has been slightly amended by ACGA to make their focus and content clearer.

should publish its audited annual results if it chooses to produce an unaudited fourth quarter report.

SCODA, meanwhile, had already stated in the discussion paper that it was against requiring any formal qualifications for CEOs and CFOs, and also did not support the proposal that an external audit firm be mandated to carry out internal audit.

> ➢ *See Appendix 3 for a detailed outline of the SEBI / SCODA discussion paper from September 2009. Note that the issue of auditor rotation is not covered in this appendix as it is covered in detail in Issue 5 of this White Paper.*

Recommendations

We believe that certain reforms are needed to improve the quality and timeliness of corporate disclosure of most listed companies in India. Such reforms would provide investors with more useful information on which to make investment decisions and would strengthen the reputation of the Indian capital market. We recommend that:

4.1 The rules relating to the publication deadlines for audited annual results (and annual reports) be clarified for companies that opt to produce an unaudited fourth quarter report (with a limited review by the auditor). All companies should, in effect, be required to produce audited annual results within three months of the year end and their full annual report within four, or at most five, months of the year end.

4.2 The format of quarterly P&L statements be reviewed to require additional details regarding revenues.

4.3 Listed companies be encouraged to provide both cashflow statements and balance sheets with their quarterly reports.

4.4 SEBI actively consults investors in both India and overseas regarding the format and content of balance sheets, P&L statements and cashflow statements, with the aim of making them more user friendly and in conformance with global standards.

4.5 Stock exchanges (NSE and BSE) become the central depository for all listed company reports, announcements, circulars and notices, and that such information be archived for 10 years.

4.6 Companies use their websites more efficiently and as a stronger communications tool for investors and other stakeholders.

4.7 CorpFiling and EDIFAR be merged into one database, with the structure following the organisation of EDIFAR, but with further thought being given as to how information could be even more easily accessible (eg, additional content categories such as "AGM / EGM Notices and Results").

Issue 5: The Auditing Profession

The Indian auditing profession is highly fragmented. It would benefit from some consolidation as well as an independent audit regulator

Like other markets around the world, India has suffered its fair share of accounting frauds over the years (see box next page), with the Satyam case being only the largest and most egregious. Not surprisingly, these frauds have made investors question not only the integrity of company accounts, but the quality of the audit profession itself. Some of the key issues are:

- Why do many audit firms in India not have sufficient depth and expertise?
- Are they large enough and experienced enough to support clients who go global?
- What is being done to address the need for more qualified auditors in the market?
- Is there an independent regulator of the audit profession?

Audit firms need more depth

India has a surfeit of audit and accounting firms, but most are sole practitioners or have less than 10 partners. According to a 2008 questionnaire[27] by Institute of Chartered Accountants of India (ICAI), "there is no hard core definition of a small and medium practitioner". However, in the context of a market like India, a small firm would typically be seen as one having less than five partners and would have a smaller number of employees and gross receipts of about Rs5m (US$ 111,000), although these numbers may vary depending upon the demographic profile of the firm. An auditor told ACGA that while there were no reliable sources as to how many small accounting and auditing firms there were in India, it was safe to say that the number ranged between 90-95% of all firms in India.

Surprisingly, even some large companies, including PSUs (public sector undertakings[28])—a number of which are listed on exchanges outside India and are Fortune 500 companies—are audited by these small firms. It is doubtful whether smaller firms have the geographical reach and depth of knowledge to handle the accounts of companies that are becoming increasingly global. It is also unlikely that they would be able to scrutinise the internal controls and risk management processes of their clients as thoroughly as they should.

As one accountant explained, smaller firms end up doing a "tremendous amount of vouching, looking at each transaction". He added that they would probably be horrified at how the bigger audit firms do things, for "we do comparatively little transaction vouching". Instead, the bigger firms "test the overall controls and document processes, and rely on IT tools to detect errors. We focus our audits on looking at the IT systems, making sure that the controls and checks and balances are spot on, and satisfying ourselves that nothing can slip through the cracks. Then you have to test a handful of transactions, for the way IT systems work is if those are correct, then every one will be correct, generally."

Some of the larger companies have been trying to convince ICAI to talk to its members about consolidating, but that has not happened. Instead, people in the audit profession say that smaller firms are beginning to form networks where work from large listed

companies is being farmed out among a number of auditing firms, including mid-size and larger ones.

Indian accounting frauds (pre-Satyam)

CRB Capital Markets: In 1996, the company's chairman, Chain Roop Bhansali, siphoned off Rs12 billion (US$337m).

ITC and Chitalia Groups: Caught violating the Foreign Exchange Regulations Act (FERA) between 1990-95 to the tune of US$80m.

Home Trade: In 2002, the company, which is a broker, was accused of causing Rs6 billion (US$124m) worth of losses due to forgery and bad investment.

Nagarjuna Finances: Executives accused in 2003 of failing to return approximately Rs1 billion to depositors in 1997-98.

Global Trust Bank (GTB): Collapsed in 2004 having been over-exposed to the capital markets and suffering huge non-performing assets. GTB tried to cover up its problems through under-provisioning, amounting to more than Rs10 billion (US$222m).

Sources: "India's Top Five Accounting Frauds", January 11, 2009, Invest in India, and "Home Truths", Frontline, Vol 19 – Issue 11, May 25-June 7, 2002.

Artificial quotas

Another particular characteristic of the Indian audit industry is the artificial and restrictive caps placed on the number of new audit trainees that firms can take on each year—a measure originally designed to protect the existence of the smaller audit firms by ensuring that the bigger firms cannot take on too many trainees.

The trainee cap for each firm is based on a formula related to its size and number of partners. The current scheme for training of students has been in force since 2007. ICAI permits, subject to certain conditions, students to be registered under partners as well as other auditors in a chartered accountant (CA) firm. For partners, the entitlement ranges from one to 10 depending on the number of years they have been practicing as CAs. For example, a partner who has continuously practiced for three years is entitled to train one student; a partner who has continuously practiced between 3 to 5 years may train three students. For firms with up to 100 chartered accountants, one student may be registered for every CA; for firms with up to 500 chartered accountants, the firm may register 100 students plus 50% of the number of CA employees in excess of 100 (maximum students 300).

This rule has hampered the ability of larger audit firms to employ a sufficient number of qualified auditors. Although these restrictions have been loosened over the years, they still exist and are a serious impediment to the development of individual firms and the industry as a whole.

The Companies Act also limits the number of partners that each audit firm may have to 20. Many argue that this increases the workload of each partner and has the potential to undermine the quality of an audit. This restriction also puts constraints on growth and

competition. The Companies Bill 2009 proposes to remove all limits for CA firms; however it is not yet clear if the Bill will be enacted without modification.
A new Limited Liability Partnership (LLP) Act 2008 became effective in 2009 and many hope that it will help to alleviate the audit-partner problem, since the Act does not restrict the number of partners that an LLP can have. However, auditors fear that ICAI will find a way to ensure it does not apply to audit firms. The current definition of LLP is ambiguous since it refers to both "a partnership" as well as "a corporate body" and the confusion arises because the Companies Act expressly disqualifies a corporate body from being appointed a company auditor. However, an accountant told ACGA that ICAI was in discussions with the Ministry of Corporate Affairs to make the necessary amendments in law to allow an audit LLP firm to be appointed a company auditor, which was seen by the profession as a positive step.

It is worth noting, however, that even if the issue of audit-partner numbers is resolved, the cap on trainees would still remain.

An independent regulatory body?
ICAI is a self-regulatory body established under the Chartered Accountants Act, 1949 to regulate the auditing profession in India. As it is an industry body, however, it is not independent from the profession that it regulates. This is why India, for example, is not a member of the International Forum of Independent Auditor Regulators (IFIAR)[*], a network of independent regulatory bodies from North America, Europe, Asia-Pacific, the Middle East, South America and other parts of the world. It is also why many Indian auditors believe that while ICAI should continue to provide educational courses for accountants and auditors (which the Institute is seen as doing well), its regulatory powers should be transferred to an independent body (as it is not seen as an effective and independent regulator). Auditors feel that India is being left behind in terms of the quality of its audit regulatory system.

ICAI defends itself against these charges. In an article in January 2009, for example, it said it had sanctioned 122 chartered accountants since 2006[29]. Until that time, however, no action had been taken by it against the auditors of Global Trust Bank (GTB), although it had been investigating the case since 2004. In February 2009, not long after the Satyam debacle, the disciplinary committee of ICAI found two of the GTB auditors guilty of "professional misconduct" and submitted a report to the ICAI Council for further action. In April 2009, Pricewaterhouse, the GTB audit firm, brought action against ICAI challenging the context of the disciplinary proceedings.

Two issues hamper ICAI's enforcement capabilities: a plethora of committees that oversee disciplinary actions and the possibility of litigation. One auditor told ACGA that because any penalty levied by ICAI could be challenged in court, the Institute can and does take a long time to decide on penalties (since it does not want to face lengthy court cases and pay exorbitant legal fees). In addition, depending on the issue, disciplinary action can go back and forth between committees before ICAI decides what action to take. An auditor noted that not all the members of a committee may be available at the same time, making meetings difficult to set up at times.

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[*]For a full list of IFIAR members, go to: www.ifiar.org

Although there have been moves in recent years to create a more independent audit regulator in India, the results have been less than impressive. In 2007, the Ministry of Corporate Affairs (MCA) constituted the ICAI Quality Review Board (QRB), which was intended to set standards for services provided by the Institute's members, review the quality of the services provided by them and ensure they adhered to the various statutory and other regulatory requirements. However, K.N Memani, Chairman of the Board, resigned his post in January 2009 following the Satyam scandal. While he refused to discuss the reasons behind his sudden resignation, there was speculation that he resigned due to a lack of support from ICAI, which was to have given funding and other infrastructural support to the QRB.[30] ICAI president at the time, Ved Jain, denied these rumours. But in October 2009, K.D Gupta, Chairman of the QRB, said in an interview that besides three meetings with ICAI, the Institute had done little to help the Board function.[31] He also said that although ICAI was to have provided funding for the Board, it had not been forthcoming, forcing the Board to approach MCA, which provided Rs500,000. ICAI will have to replenish this once the fund is exhausted.

An independent audit regulator would not only bring India closer to international norms in this area, but it could help to find solutions to a host of problems that audit firms face. It is a common practice, for example, for auditors not to independently verify the bank statements of client companies, but instead to rely on bank account information provided by clients. Auditors in India say that banks, remarkably, will not respond—promptly or at all—when asked for such information. One audit partner said he has to send staff to banks to get company documents verified and instructs them to sit and wait until the work is done.

SEBI policy reform

Regulators in India have begun thinking about issues relating to audit quality and independence over the past year. For example, in a discussion (consultation) paper SEBI released on September 14, 2009 on proposed changes to the Listing Agreement, one of the reforms suggested was the rotation of either audit firms or audit partners as a way to enhance their independence from clients.

SEBI felt that the independence of auditors should be reviewed because, as it said in its discussion paper:

> "The quality of financials reported by companies and the true and fair view of the financial statements submitted by listed entities to the stock exchanges have, of late, come into sharp focus."

It argued that while auditors were technically appointed by shareholders at annual meetings, "in practice, the shareholders merely approve a set of names that are proposed/nominated by the Board of Directors and the promoters, who may be a part of the Board". Moreover, the "Board of Directors and the promoters may ensure that the firm they wish to appoint is approved in the meeting, in view of the sheer strength of their voting powers".[32]

SEBI also said that a long association between an audit firm and a listed company could lead to "complacency and defeat the true sense of independence of the auditors". It therefore asked the Standing Committee on Disclosures and Accounting Standards (SCODA), a committee that advises SEBI on financial and accounting policy, to consider

whether there was a need to set new rules on the mandatory rotation of audit firms or the mandatory rotation of the partners of an audit firm.

SCODA concluded that the "mandatory rotation of (audit) firms may not be practical by all (listed) companies" and recommended that:

- "SEBI may mandate that the partner of the audit firm signing the audited accounts of a listed entity be mandatorily rotated every five years."

And:

- "The Audit Committee shall be responsible for ensuring independence of the audit firm and its partners."[33]

SCODA said that the aim of these recommendations was to ensure that external auditors were independent from management and to break any long-term association between audit partners and the management of listed entities.

As of November 9, 2009, when the SEBI Board last met to approve various reforms to the Listing Agreement (*see Issue 4: Corporate Disclosure*), the rotation of audit firms and/or partners was not on the list.

Recommendations
We believe that certain reforms are needed to strengthen the audit profession in India and the way in which it is regulated. Such reforms would improve the quality of audit, the integrity of information provided to investors and the reputation of the Indian capital market. We recommend that:

5.1 Indian chartered accountant (CA) firms be allowed, and encouraged, to consolidate. This would enhance the depth of skills in the profession and provide a firmer basis for audits of listed companies. This would also strengthen India's goal of turning Mumbai into an international financial centre.

5.2 Artificial caps on the number of audit trainees and audit partners be removed.

5.3 The Government establish an independent regulatory body for the audit profession. Such a body could draw its talent from among the many experienced auditors in India, including those who have worked overseas.

5.4 The SEBI Board approves SCODA's recommendations on the mandatory rotation of audit partners and the clarification of the audit committee's responsibilities regarding auditor independence.

We also recommend that the Government and securities regulator proactively consult institutional investors and other market participants in India and overseas as they move forward on any reform of the audit profession. Such consultation could be carried out in part through existing corporate governance organisations, such as ACGA or ICGN (the International Corporate Governance Network), or through more specialised entities such as the Global Auditor Investor Dialogue, an informal forum comprising the major auditing networks and global investors.

Appendix 1: Shareholder Meeting and Results Data in India

Indian Oil 2007 Annual Meeting		
Resolutions	**Votes in favour (No. of shares)**	**Votes against (No. of shares)**
Item 3: Reappointment of Shri Vineet Nayyar as director	967,099,010	11,641
Item. 5: Reappointment of Shri B. M. Banasal as director	967,098,460	11,641
Item 6: Reappointment of Shri S. V. Narasimhan as director	967,097,210	11,641
Item 12: Approval to the IOC-IBP merger scheme trust	967,099,010	11,641

Source: Indian Oil

Company	Latest AGM Results
Reliance Industries	Results of 2009 AGM published on BSE on November 19, two days after the AGM.
Oil & Natural Gas Corp (ONGC)	Minutes of 2009 meeting on BSE and NSE websites. AGM held on September 23, but minutes only posted on October 21, 2009 on NSE, but made available on BSE on September 23.
Bharti Airtel	Summary of 2009 results on BSE and NSE websites on August 21, the same day as the AGM.
NMDC	Results of 2009 AGM not published.
Infosys Technologies	Transcript and archived webcast of its entire 2009 AGM is available on the Infosys website, but not on the exchange websites.
State Bank of India	Results of 2009 AGM not published.
DLF	Summary of 2007 AGM results on NSE website, but not 2008 or 2009 AGM results.
Kotak Mahindra	Minutes of 2009 AGM on BSE and NSE websites. AGM held on July 28, but minutes only posted on August 10, 2009.
Wipro	Minutes of 2009 AGM on BSE and NSE websites. AGM held on July 19, but minutes only posted on August 27, 2009.

Source: ACGA research

Appendix 2: Format of Quarterly Reports

(Rs. In lakhs)

Particulars	3 months ended (dd/mm/yyyy)	Corresponding 3 months ended in the previous year (dd/mm/yyyy)	Year to date figures for current period ended (dd/mm/yyyy)	Year to date figures for the previous year ended (dd/mm/yyyy)	Previous accounting year ended (dd/mm/yyyy)
	Audited/ Unaudited*	Audited/ Unaudited*	Audited/ Unaudited*	Audited/ Unaudited*	Audited/ Unaudited*
(a) Net Sales/Income from Operations (b) Other Operating Income					
2. Expenditure a. Increase/decrease in stock in trade and work in progress b. Consumption of raw materials c. Purchase of traded goods d. Employees cost e. Depreciation f. Other expenditure g. Total (Any item exceeding 10% of the total expenditure to be shown separately)					
3. Profit from Operations before Other Income, Interest & Exceptional Items (1-2)					
4. Other Income					
5. Profit before Interest & Exceptional Items (3+4)					
6. Interest					
7. Profit after Interest but before Exceptional Items (5-6)					
8. Exceptional Items					
9. Profit (+)/ Loss (-) from Ordinary Activities before tax (7+8)					
10. Tax expense					
11. Net Profit (+)/Loss(-) from Ordinary Activities after tax (9-10)					
12. Extraordinary Item (net of tax expense Rs……..)					
13. Net Profit (_)/Loss(-) for the period (11-12)					
14. Paid-up equity share capital (Face Value of the Share shall be indicated)					
15. Reserve excluding Revaluation Reserves as per balance sheet of previous accounting year					
16. Earnings Per Share (EPS) (a) Basic and diluted EPS before Extraordinary items for the period, for the year to date and for the previous year (not to be annualized) (b) Basic and diluted EPS after Extraordinary items for the					

period, for the year to date and for the previous year (not to be annualized)					
17. Public shareholding - Number of shares - Percentage of shareholding					
18. Promoters and Promoter Group Shareholding ** a) Pledged / Encumbered - Number of shares - Percentage of shares (as a % of the total shareholding of promoter and promoter group) - Percentage of shares (as a % of the total share capital of the company) b) Non - encumbered - Number of shares - Percentage of shares (as a % of the total shareholding of the Promoter and Promoter group) - Percentage of shares (as a % of the total share capital of the company)					

Appendix 3: SEBI Policy Reform 2009

Details on the SEBI discussion paper of September 14, 2009, and the response of the Standing Committee on Disclosures and Accounting Standards (SCODA), are as follows:

Note: This appendix omits the discussion on auditor rotation, as that was covered in detail under Issue 5 of the "ACGA White Paper".

- **Professional qualifications / financial literacy of CEOS and CFOs**: Current regulations—Clause 49 of the Listing Agreement—require that the CEO and CFO certify that they have reviewed the financial statements for the year and that, to the best of their knowledge, the statements do not contain any false or misleading information. But regulations do not specify whether the CEO or CFO needs any specific educational qualification. In the wake of the Satyam scandal, SEBI asked SCODA to deliberate on whether there was a need to require CEOs and CFOs to have certain minimum professional qualifications and financial literacy.

  SCODA concluded that it might not be appropriate for SEBI to specify particular professional qualifications for a CEO, as companies prefer them to have relevant industry experience. Even for CFOs, the Committee refrained from recommending any minimum professional requirements, saying instead that it should be the responsibility of the audit committee to appoint someone capable.

- **Appointment of an external audit firm as an internal auditor**: Clause 49 requires that the audit committee review, with management, the performance of both the statutory (ie, external) and internal auditors, as well as the adequacy of the internal audit function, if any, including the structure of the internal audit department, reporting structure coverage and the frequency of internal audit. The audit committee should also review the internal audit reports relating to internal control weaknesses and discuss significant findings with the internal auditors. Currently, the appointment, removal and terms of remuneration of the chief internal auditor should also be reviewed by the audit committee. These provisions were inadequate, SEBI felt, following the Satyam scandal. Instead it proposed that internal audits should be carried out by an external audit firm to ensure the internal control systems of a company were truly independent and not influenced by management.

  SCODA, however, recommended against such a move, stating that the current requirements in Clause 49 were adequate.

- **Qualification in auditor's report relating to disclosure of promoter shareholdings**: On February 3, 2009, SEBI amended the Listing Agreement to require companies to provide additional details in their periodic financial reports on the shareholdings of promoters and promoter groups, including information on pledged and unencumbered shareholdings. This led to some concern as to whether investors might think that this information had been reviewed and certified by the auditors. The recommendation from SCODA was that the following could be added at an appropriate place in the auditor's report:

"except for disclosures in item No. 17 and 18 namely, 'Public Shareholding' and 'Promoter and Promoter Group Shareholding', which have been traced from disclosures made by the management".

- **Voluntary adoption of IFRS by subsidiaries of listed entities**: The Ministry of Company Affairs tentatively announced in 2008 that Indian financial reporting standards would converge with IFRS by 2011. To prepare for this, it was thought necessary to give listed companies sufficient lead time to come to terms with IFRS requirements. SCODA's discussion of the possibility of voluntary adoption of IFRS by companies for consolidated accounts led to two alternative views:

  - Allowing only listed companies that have overseas subsidiaries contributing a major portion of total revenue of the consolidated entity—at least 50%—to be given the option of voluntarily adopting IFRS; or
  - Allowing all listed entities having subsidiaries to voluntarily adopt IFRS by 2011.

- **Interim disclosure of balance sheet items by listed entities**: Section 210 of the Companies Act requires all registered companies to provide shareholders, during the AGM, a balance sheet containing a statement of assets and liabilities as at the end of the financial year. While Clause 31 of the Listing Agreement requires listed companies to forward copies of their balance sheets to the stock exchanges, neither the Companies Act nor the Listing Agreement requires companies to submit balance sheets on a quarterly or even half-yearly basis. Following the global financial crisis and the bankruptcy of some global corporations, SCODA said that more frequent disclosure of the asset-liability position of companies would assist shareholders to assess their financial health. It recommended that listed companies should disclose balance sheets on a half-yearly basis.

- **Timelines in submission of financial results by listed entities**: The various timelines laid down by SEBI for submitting annual and quarterly financial results are quite confusing. In order to streamline these, SCODA made six recommendations:

  - Quarterly audited financial results (unconsolidated) and quarterly unaudited results (unconsolidated) accompanied by a limited review from an auditor should both be submitted within 45 days of the quarter end. This would be applicable for all quarters except the last quarter.

    Note: Previously different deadlines applied to quarterly reports (one month) and the limited review report (two months).

  - Listed companies with subsidiaries would, in addition to the above, have to submit consolidated audited quarterly results, or unaudited quarterly results accompanied by a limited review report, within 45 days from the end of the quarter. Again this would hold true for all quarters save the last one.

- Listed entities that have subsidiaries and that submit consolidated quarterly results in addition to stand-alone (unconsolidated) results shall in future publish only consolidated financial results. However, the following items shall also be published on a stand-alone basis as a footnote: (a) turnover (b) profit before tax (c) profit after tax.

- Listed entities which opt to submit their audited annual results on a stand-alone (unconsolidated) basis in lieu of the last quarter unaudited financial results (with a limited review report by the auditors) shall submit the annual audited results within 60 days from the end of the financial year.

- Listed entities with subsidiaries shall, in addition to submission of stand-alone audited annual results as mentioned above, submit their consolidated audited annual results within 60 days from the end of the financial year.

- Listed entities that do not opt to submit their audited annual results within 60 days from the end of the financial year, as mentioned above, shall submit their fourth quarter unaudited results (accompanied by limited review) within 45 days from the end of the quarter.

Appendix 4: About ACGA

The Asian Corporate Governance Association (ACGA) is an independent, non-profit membership association dedicated to promoting long-term improvements in corporate governance in Asia through research, advocacy, and education.

ACGA carries out independent research in 11 major Asian markets. It engages in a constructive and informed dialogue with regulators, issuers, institutional investors and other key interest groups. And it organises educational events, including an annual conference, to raise awareness and provide a forum for discussion of timely corporate governance issues.

ACGA is known for its "White Papers" and "Statements" on regulatory reform in different Asian markets (eg, India, Japan, Singapore) and its regular "CG Watch"* survey of corporate governance in Asia—first undertaken in 2003. It has also developed a website, **www.acga-asia.org**, providing a wide range of data and analysis on corporate governance conditions and regulations in major Asian markets.

(*Carried out in collaboration with CLSA Asia-Pacific Markets, a Founding Sponsor of ACGA)

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Endnotes

[1] Like the US, quorum requirements in Japan are high, necessitating a large proxy solicitation industry to ensure sufficient votes of domestic and foreign shareholders are cast at meetings. In contrast, quorum rules in common law jurisdictions such as Hong Kong, India, Malaysia and Singapore are low—just two or five members—hence there is no proxy solicitation industry.

[2] These include, for example: Aberdeen Asset Management Asia in Singapore; bcIMC in Canada; the California Public Employee's Retirement System (CalPERS), the California State Teachers' Retirement System (CalSTRS) and TIAA-CREF in the US; F&C Asset Management, Hermes Investment Management, RAILPEN Investments, and Standard Life Investments in the UK; PGGM Investments in the Netherlands; and Norges Bank Investment Management in Norway.

[3] "ACGA Asian Proxy Voting Survey 2006", p11

[4] In an interview with ACGA.

[5] Companies Act, 1956: Section 176

[6] Companies Act, 1956: Section 179

[7] There are no dedicated proxy agents in India, rather they are vendors that custodian banks use for other services, such as debt collection. These vendors, which have offices around the country, are trained by the banks how to handle proxy votes at AGMs.

[8] Postal ballots are carried out on special resolutions such as alteration in the Object Clause of Memorandum. Full description of postal ballot resolutions is available in the Appendix.

[9] Interview with ACGA in 2009.

[10] Interview with ACGA in 2009.

[11] Companies Bill, 2009, Section 94.

[12] Companies Bill, 2009, Section 98 (5)

[13] The Stock Exchange of Hong Kong, Listing Rule 14A.01

[14] The Stock Exchange of Hong Kong, Listing Rule 14A.03

[15] Singapore Exchange Listing Manual, Chapter 9, Rule 901

[16] Singapore Exchange Listing Manual, Chapter 9, Rule 906

[17] Campbell R. Harvey, 2004. Found at: http://financial-dictionary.thefreedictionary.com/warrants

[18] "Dictionary of Financial Terms", Lightbulb Press, 2008. Found at: http://financial-dictionary.thefreedictionary.com/warrants

[19] Harvey, 2004. (As above)

[20] SGX Listing Manual, Chapter 8, Part IV, 809.

[21] SGX Listing Manual, Chapter 8, 812(1).

[22] The Stock Exchange of Hong Kong, Listing Rule 13.36(2)(b) and 14A.31(3).

Note: The SEHK listing rules also state that, as a matter of principle, no securities may be offered to directors of a new listing applicant or their associates "on a preferential basis" and "no preferential treatment" may be "given to them in the allocation of the securities". Rule 10.03 and 10.03(1)

[23] "Dematerialised" securities are paperless securities that exist only in the form of entries in the book of depositories. The system works through a depository who is registered with the Securities and Exchange Board of India (SEBI) to perform the functions of a depository as regulated by SEBI.

[24] "Relevant date" means:

(a) In the case of preferential issue of equity shares, the date thirty days prior to the date on which the meeting of shareholders is held to consider the proposed preferential issue;
(b) In case of preferential issue of convertible securities, either the relevant date referred to in clause (a) or a date thirty days prior to the date on which the holders of the convertible securities become entitled to apply for the equity shares.

[25] "A warrant to arrest the abuse of warrants", CNBC-TV18, Aug 7, 2009.

[26] To date listed companies in India have to produce a quarterly financial report (audited or unaudited) within one month of the end of each quarter. There are two options for the fourth quarter:

1. Produce an unaudited report within 30 days of year-end (with a "limited review" by your auditor within 60 days of the year-end), followed by a full annual report with audited annual results ('when the board approves them'). Or:
2. Produce audited annual results for the full year within 90 days of year-end.

In November 2009, the SEBI Board indicated that it would be making various amendments to the Listing Agreement, including some changes to the timelines for submission of financial results. The final have yet to be published.

[27] Questionnaire on changing profile of profession, ICAI, December 15, 2008

[28] State-owned enterprises

[29] "Bringing Satyam auditor PwC to book may not be easy", IBNLive, Jan 9, 2009

[30] "ICAI Quality Review Board chief Memani quits", Times of India, January 23, 2009

[31] "ICAI keeps board to review members' services at bay", Indian Express, October 29, 2009

[32] "Discussion paper on proposals relating to amendments to the Listing Agreement", Securities and Exchange Board of India (SEBI), September 14, 2009, page 2.

[33] Ibid