A Comparative Analysis of the Rights of Shareholders in India and the United Kingdom

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Introduction

The rights of shareholders form the cornerstone of the corporate structure. Shareholders' rights refer to the legal entitlements of shareholders vis-à-vis companies in which they invest[1]. These rights are, and always have been, primarily the result of private agreements that have been subjected to various forms of explicit and implicit control. This legal framework provides major normative benefits by facilitating the creation of innovative and efficient corporate structures.[2] Shareholders are the risk capital providers; therefore, they must be able to protect their investment by confirming that the company is managed by a competent board of directors and that effective strategies for the company's overall corporate performance and long-term sustainability are in place. Boards should serve the company's shareholders equitably by respecting the rights of the investors. The Board should work towards ensuring that the shareholders are able to exercise their rights and that unnecessary barriers are not erected by which the exercise of ownership rights by the shareholders is impeded. The rights of shareholders can therefore be understood better by way of a comparative analysis of the legislative provisions surrounding their rights in India and the United Kingdom. The company law in India is heavily influenced by the laws of the United Kingdom, so several of the Indian laws owe their origin to British legislation. Both countries present striking resemblances with regard to the safeguards provided to secure the varied rights that are available to the shareholders. And yet we notice inherent differences in the articulation of these rights. Therefore, it becomes crucial to understand the fundamentals of these rights in each of the two nations.

Shareholder's Rights in the UK

While the responsibility of managing a company lies with the directors, the ownership of the company lies with the shareholders. The rights of the shareholders in the United Kingdom have therefore been enshrined in the Companies Act, 2006[3] *(hereinafter referred to as 'CA')*. In the UK, limited companies can be either private or public. While the latter's liability is limited solely by shares, the former's liability can be limited by shares or a guarantee. The articles of association *(hereinafter referred to as 'AOA')* lay down the rights of the shareholders. The different classes of shares in a company influence the rights of shareholders pertaining to different shares. These rights are frequently spelled out in the AOA of the company. A company has absolutely no prescribed numeric limit in relation to the different classes of shares it can have. Despite the fact that ordinary shares are the major category of shares that are issued by a company, entitling dividends, payment on winding up of the company and participation in the meetings of the dividends, payment on winding up of the company and participation in the meetings of the company to the shareholders,[4] shares may as well be in the form of preference shares, convertible or differed shares, redeemable or non-redeemable shares, etc.

The basic rights of shareholders in UK are usually the same for both public and private companies. There are certain special rights that can be conferred on the shareholders. By passing an ordinary resolution at a general meeting, shareholders can appoint directors to the board. Under Section 160(1) of CA, in the absence of a resolution allowing the passing of a single resolution, separate resolutions must be passed for each appointment, if more than one director is to be chosen[5]. Shareholders can remove directors through an ordinary resolution under Section 168(1), notwithstanding any provision to the contrary in any agreement between the company and the director[6]. Section 21(1) also empowers the shareholders to compel the Board of Directors *(hereinafter referred to as 'BOD')* to undertake a certain course of action by way of a special resolution that modifies or overrides the company's AOA.[7] While the rights of the shareholders' can be restricted, amended, or even done away with, the shareholders' can, in no circumstance, be held accountable beyond the amount owed on their shares. However, in certain exceptional situations under Section 847(1) and (2), the shareholders are obligated to repay the company if they know or have reasonable grounds to believe that they have received an unlawful distribution.[8] Shareholders can agree to limit their rights to the company and/or among themselves. But in circumstances where there is more than one class of shareholders, the articles are usually framed in such a way that, in the absence of the approval of one class of shareholders, their rights cannot be changed by changing the rights of another class.

In the UK, the rights of the shareholders are contingent on the percentage of shares/voting rights they hold in the company. This distribution of rights can be demonstrated as follows:

Shareholders possessing:

1. At least 5% of the shares: They have the right to approach the court to prevent the conversion of a public company into a private one. Section 303(2) of the CA allows them to call a general meeting.[9] Section 292 mandates that a written resolution be circulated to such shareholders.[10] Under Section 314 of the CA, the shareholders can require the company to circulate the statements with regards to the matters or business to be dealt with at the meeting.[11]

2. At least 10% of the shares: In addition to the above-stated rights, Section 476 of CA allows such members to force the holding of audits for a financial year.[12] They also have the capacity to demand a poll in respect of a resolution under Section 321.[13]

3. More than 10% of the shares: In addition to the above stated rights, in the case of private limited companies, they can prevent a meeting scheduled on short notice under Section 307.[14] Section 979[15] also empowers them to block squeeze outs.[16]

4. At least 15% of the shares: In addition to the above stated rights, Section 633 of the CA grants the right to approach the court to have a variation of class rights cancelled if the affected shareholders did not consent to or vote in favour of the change.[17]

5. More than 25% of the shares: In addition to the above-stated rights, they have the power to block special resolutions and schemes of arrangement.

6. At least 50% of the shares: In addition to the above-stated rights, Section 282 grants the right to block ordinary resolutions.[18] Because ordinary resolutions are connected with a company's general management, the capacity to block them can obstruct the business's day-to-day operations.

7. More than 50% of the shares: In addition to the above-stated rights, such shareholders are granted the right to pass ordinary resolutions under Section 282 of the CA.[19]

8. At least 75% of the shares: They are granted the right to pass (i) special resolutions under Section 283[20] and (ii) schemes of arrangement under Section 899.[21]

9. At least 90% of the shares: Under Section 307 of CA, such shareholders have the right to call for a short notice meeting in a private limited company. [22] But this figure rises to 95% in respect of public limited companies.[23] They also possess the right to pass squeeze out under Section 979.[24]

Specific circumstances also allow the shareholders to bring actions against the directors. For example:

- In the event of negligence, breach of duty, default, or breach of trust by a director, a derivative claim can be filed by the shareholder on behalf of the company. This, however, is contingent on the approval of the court.
- In the case of an "unfair prejudice" claim, minority shareholders can not only file this but also seek redressal for the company's controlling directors' actions. Alternatively, the shareholders may seek the winding-up of the company on grounds of oppression.
- In situations where a personal cause of action by the shareholder against the director arises.
- In cases where the director of the company not only violated the constitution of the company, but such an action can in no way be ratified by the shareholders.

With regards to the shareholder's approval required for certain issues in a general meeting, in the case of private companies, approval in a meeting must be sought only when it involves the removal of directors and auditors. While the advantage of the written resolution route is accessible to private companies, its availability is absent for public ones. Further, for listed companies, certain transactions necessitate the approval by shareholders at general meetings. A few examples can be of a "related party transaction," that is, a transaction involving the company and a director, a key shareholder, a "person exercising significant influence," or someone who is associated with them and one of the percentage ratios (profits, gross capital, gross assets and consideration) is more than 25%, which is a "Class 1" transaction.[25] Auditors can be appointed by the directors or shareholders of both public and private companies by passing an ordinary resolution. In the UK, each person represents one vote, and it takes place by a show of hands unless there is a demand for a poll. In this case, each shareholder has one vote for each share that they own. There is also a provision for a proxy vote in place of an in-person vote, which carries the same weight. Therefore, we notice that the rights of the shareholders are not only well pronounced but also efficiently equipped in the United Kingdom.

Shareholder's Rights in India

The Companies Act[26], 2013 *(hereinafter referred to as 'the Act')* is by and large the primary source in India under which companies are established and regulated. Private limited companies and public limited companies are two substantive categories of companies incorporated in India, which are restricted either by shares or by guarantee. Various factors come into play while dealing with the choice of entity (public or private), even though India has relatively more private limited companies. Equity shares and preference shares are the two major categories of shares issued, both of which accord their holders participating rights. Debentures, bonds, warrants, stocks and others by no means exercise participative rights in a company, even though they are issued by that particular company. By considering Section 3(1) of the Act, the type of a company decides the lowest number of shareholders. For instance, a single-person company has one shareholder, while a private limited company and a public limited company have two and seven shareholders respectively.

A few sector-specific legislations necessitate a separate and distinct form of entity to be incorporated, especially when we talk about insurance companies in India, which are indispensably amalgamated as a public limited company. The usual trend observed in cases of foreign investors is their preference to incorporate a private limited company in the country, contingent on the restrictions of the particular sector. This is not only because private limited company are exempted from some compliance but also due to their freedom to lay down limitations on a transferability of shares, thereby resulting in consistent ownership and control granted to the foreign investors. Shareholders play a significant part in both the companies and are, therefore, granted varying rights and safeguard under the Act.

Shareholders have significant influence on a director's selection, who is basically responsible for supervising all major affairs of a company. Section 152 of the Act deals with the appointment of directors in a company.[27] An ordinary resolution passed by the shareholders is the norm for the appointment of different kinds of directors, as set forth in Section 161 of the Act, which includes Nominee Director, Alternative Director, and Additional Director. In certain instances, the Board, as a collective body, has been conferred with the right to appoint a director. However, the same is for a limited period, beyond which the approval of shareholders is mandatory.

A fiduciary duty is carried by the directors towards the shareholders of the company they work for and the company itself.[28] Any resolution of the BOD, that adversely affects the interests of the company or is prejudicial to the welfare of the company can be challenged by reason of mismanagement. The Companies Act, 2013 has provisions which clearly summarise the situation where shareholders' rights can be exercised to prosecute directors of a company. These include situations where a director's act is not only detrimental to the affairs of the company but also in violation of the charter documents. Other situations involve circumstances of fraud, property of the company being transferred at a low valuation, diversion of business money, or any act which is mala fide in nature.[29]

Chartered Accountants are responsible for reviewing the account, performing internal audits, assessing the company's profit and loss accurately and monitoring the laws in place. This provides outstanding defence for the shareholders. Section 139 of the Act bestows the privilege of selection of the company's first auditors on the BOD, but for a limited timeframe of one year, and then, on the suggestion of the BOD and audit committee, the shareholders appoint the auditor at the Annual General Meeting *(hereinafter referred to as 'AGM')*, which is usually for a period of five years.

Whichever issue a company is constitutionally able to deal with, a right to vote on such an issue is held by shareholders because the vote is believed to be a property right in the name of the shareholder which he can exercise as he sees fit. To do so, a shareholder may have to attend and vote in the general meeting and the voting rights of two types of shareholders, namely preference and equity shareholders, are mentioned in Section 47 of the Act. Pursuant to Section 105 of the Act, a proxy can be appointed by a shareholder who votes on his behalf only by way of a poll, even though, in the general meeting, their presence is by no means considered within the framework of the quorum.[30]

Shareholders have the unequivocal right to order the company's director to call an annual general meeting under Section 96 of the Act and may also request the coordination of a general body meeting to the National Company Law Tribunal in case the same is not accomplished in acquiescence with the regulatory stipulations. Resolutions requiring the permission of the company's shareholders include issuing sweat equity and bonus shares; amending the company's charter documents; buy-back of shares of the company; reducing the share capital, issue of debentures; remuneration of directors; appointment and removal of directors; increase in borrowing powers; sale of an undertaking; entering into a compromise or arrangement; so on and so forth.

Shareholders in a company are guaranteed certain additional rights. A minimum of 10% of the company's shareholders with voting rights also possess the right to requisition the directors to convene a general meeting. If there is a failure on the part of the directors to do so, then shareholders by themselves can call for a meeting. In the event that persons who hold a minimum of 10% of a class of shares and have their rights varied do not consent to such variation, they are entitled to move before the Tribunal to obtain a variation of rights connected to their shares rescinded. Section 241(1) of the Act accords a right to any member having 10% of issued share capital or a minimum of 10% of total member's number to broach the matter with the Tribunal when the business of that company is carried out in either an oppressive way to any member of the company or prejudicial to the public or company's interest. Further, a class action suit can be undertaken, under Section 245 of the Act, by

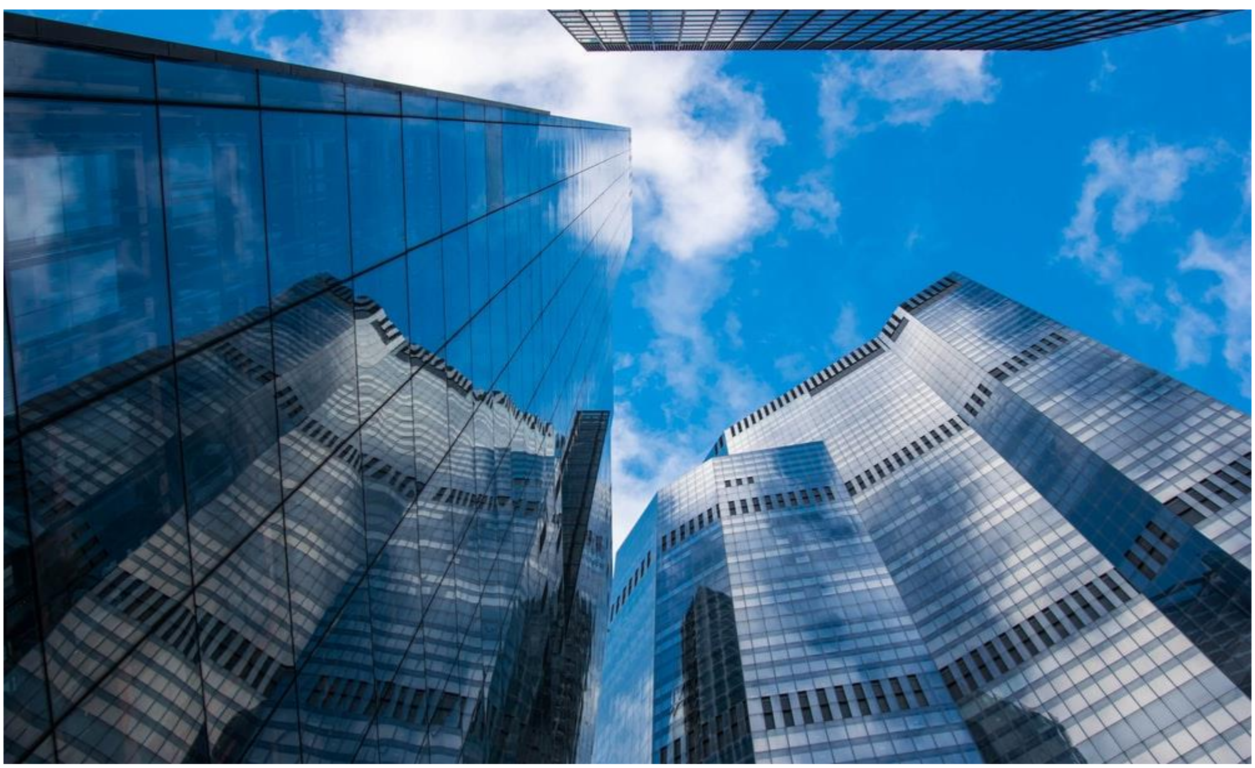
i. At least 100 members or 5% of the total number of members, whichever is less.
ii. At least 2% or 5% of issued share capital in a listed or unlisted company, respectively.
iii. At least one-fifth of the total number of members in the case of a company not having share capital.

Comparative Analysis

The statutory provisions surrounding the rights of shareholders in both countries have a comparable array of legal attributes and encounter a substantially similar array of legal issues. It becomes crucial to highlight that 'shareholder' has not been expressly defined in the Companies Act, 2013 as enforced in India. The term 'member'[31] is used broadly to outline shareholders, even though both are significantly different. A similar situation exists in the UK, where we notice an absence of a conclusive definition. In India, there is a lower limit to the number of shareholders, which varies subject to the type of the company, ranging from one-person company, private limited company, and public limited company, wherein the limit is one, two and seven, respectively. However, there is no requirement for a certain minimum number of shareholders in the UK as single-member companies can exist in both the private and public sector.

A company's first auditor in India is appointed by its BOD at the company's first board meeting, as provided under the Act, and subsequent auditors, with the reference from the BOD or audit committee, are appointed by the shareholders at the AGM. This appointment lasts for an interval of five years at a time. The appointment of auditors in the UK is carried out either by the directors or the shareholders through an ordinary resolution, in a private company. The appointment is made by the director to fill a vacancy or the first appointment can be made by a simple majority of shareholder approval, within a stipulated period of time. The audit firm will stay in place until the shareholders notify the company that they intend to terminate the appointment. Similarly, both the directors and shareholders can appoint the auditors in the case of a public company. Section 140 of the Companies Act, 2013 highlights that, right before the expiry of its term, the removal of an auditor from his/her office can be initiated by a company in India by way of passing a special resolution along with acquiring the mandatory authorization from the central government of the country. In the UK, however, a shareholder can remove an auditor in a general meeting at any time by passing an ordinary resolution.

A suit can be filed by the shareholders as members of the company, against a director in India, for those times when they are seen as not undertaking measures to implement the interests of the company and where cases of breach of duty, fraud, undervaluing assets, diversion of funds and so on are displayed. In the UK, situations which allow the shareholders to bring actions against the directors include breach of duty or breach of trust attributable to the director; default; negligence; unfair prejudice exercised by the director; violation of the charter documents without due ratification of the shareholders etc. Voting methods such as voting by show of hands and by polls are common in India and the UK. Likewise, in both jurisdictions, there exist provisions for shareholders to appoint proxy voters on their behalf.



By delving deeper into the comprehensive codes for company law in India and the UK, we notice the influence of customs and traditions, though both the statutes have evolved themselves according to the changing circumstances. While India was quick at revising its laws governing corporate structure, the UK exhibited a slow progression in this direction. This may be due to the simple reason that several provisions of the Companies Act, 2013, as enforced in India, had their roots embedded in the assumptions of the nineteenth century. The Ease of Doing Business report of 2017 by the World Bank indicated a perfect 10/10 score when it comes to protecting the rights of minority shareholders, leaving the UK behind, which scored 7/10, and hence ranked lower than India in this regard. However, we notice that in the UK, there exists a clear demarcation of the rights of shareholders based on the percentage of shares owned by them. However, such a distinction disappears in the Indian context, where varying rights can be accorded to the minority shareholders. This is a provision that India can adopt from the UK in the long run. While granting rights to shareholders, it is critical to maintain a system of checks and balances. Allowing them to remove the auditors by way of a general meeting can prove to be detrimental to the interests of the company. The Indian legislators were farsighted in this regard and hence created special requirements for undertaking such a strict measure. At this point, we conclude that, despite their many similarities, there is still room for both laws to learn their own sets of lessons from their counterparts.

Conclusion

The twenty-first century demonstrates a trend where greater attention is given to the issue of shareholders' rights by regulators, stakeholders, and the public at large. The importance of the rights of the shareholders is well understood in Indian and English law. The fundamental uniformity of the corporate structure is astonishing, despite the evident differences across jurisdictions along these lines. The parallels found in the rights of shareholders in the two jurisdictions are an indication of the growing importance of these rights in the corporate world. Both English and Indian law emphasise the wide range of rights available to the shareholders. These include but are not limited to the right to obtain dependable and timely information regarding the functioning of the company; the ability to elect and dismiss members of the board of directors; and the right to share in the company's earnings. We further notice that the classification of the companies as private and public, along with their limitation by shares and guarantees, in both countries indicates the similarity in the very basic structure. Though there exists a variation in terms of the rights accorded to different classes of shareholders, their powers to bring actions against the directors more or less coincide.

The manner in which the right to vote is exercised is also consistent in both countries. However, despite the congruences, when compared, certain provisions of Indian law appear to be more flexible and liberalised, while on the other hand, several other provisions of UK law exhibit a more expansive and accommodative approach in terms of enhancing and protecting the company's and shareholders' rights and interests. In the end, it becomes essential to understand that the corporate structures around the world are still evolving, with a long history of amendments to the various statutes involving company law and the ever growing need to conserve the rights of shareholders. Borrowing and learning from across different nations becomes especially important now more than ever.

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