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NAVIGATING EQUITY INVESTMENTS AT DIFFERENT STAGES OF CAPITAL GROWTH

AN ANALYSIS OF GOOD GOVERNANCE “BEST PRACTICES” FROM AN INDIAN AND GLOBAL PERSPECTIVE

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**Navigating Equity Investments at Different Stages of
Capital Growth:
An Analysis of Good Governance “Best
Practices” from an Indian and Global Perspective**

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TABLE OF CONTENTS

Introduction.....	3
Background and Significance	3
Objectives	3
Methodology.....	4
Legal & Regulatory Framework Governing Good Governance Practices in India:	5
Overview of Key Indian Laws & Regulations.....	5
AIF Structures and Their Regulation by the SEBI	6
Governance and Reporting Requirements under the SEBI:	6
(2) Corporate Structure and Flow of Funds:	7
Challenges and Governance Enhancements	11
a) Corporate Best Practices:.....	11
b) Applying the ILPA Principles to Enhance Corporate Governance:.....	14
Comparative Analysis and Best Practices in India and Global Contexts:	17
Comparative Overview:	17
Lessons Learned from Global Practices:	19
Conclusion:	20
(a) Summary of Key Findings:	20
(b) Future Directions:.....	20
References.....	22

INTRODUCTION

Background and Significance

The role of equity investments in India, is very important in the economic prospect of raising capital and expanding business by private Indian companies. Operating under the regulatory authority of the Securities Exchange Board of India (SEBI,) India's capital market has registered a marked rise in IPO activity due to foreign investors and the increased start-up culture. Moreover, Environmental, Social, and Governance (ESG) principles that appeal to investors to adopt sustainable business practices have also increased in importance in recent years. Thanks to strong regulations that are fully compliant with the global ones, India is considered one of the most favorable targets for private equity investors that are interested in sustainable projects. In order to decipher these IPO structures and frameworks, coupled with understanding ESG policies within India's complex market, the developments must be placed in a global setting.

Objectives

This study will assess the stages of capital growth leading up to the issuance of an IPO, keeping in mind the respective roles of the founders, private investors, end-users and most importantly, the role of venture capital funds operating in India (hereinafter referred to generally as the "India Venture Capital Fund" or ("IVCF")). This paper will review the importance of good governance at each stage of the capital growth of the private Indian company that is the "investee" of IVCFs, with a view to creating an appropriate regulatory environment for all of the actors. This paper will demonstrate the need for clear regulations in terms of transparency, investor protection, and corporate governance issues in India. The analysis will start with a discussion of the regulatory

framework of the Securities and Exchange Board of India (SEBI). The SEBI principles will then be applied to all four (4) stages of capital growth of the investee company in terms of enhancing the “corporate good governance” in all of these stages.

In addition, the paper will critically analyze the Indian legal regime in comparison with global standards as set forth by three (3) critical international bodies: namely, the International Finance Corporation (IFC), a member of the World Bank Group, the Institutional Limited Partners Association (ILPA), and Norfund, a development finance institution established by the Norwegian Storting in 1997 and owned by the Norwegian Ministry of Foreign Affairs. Therefore, the aim of this paper is to bring out the dynamics between the regulatory structure and the private equity business models of sustainable investment in India, and offer perspectives on how current trends and challenges in Indian equity investments, including in the IPO space, mirror and support global trends in this space.

Methodology

This study utilizes comparative law analysis to examine the current Indian IPO regulations vis-à-vis international norms. The research methodology also involves the qualitative analysis of the regulations impacting private equity investment in India that, especially in light of regulations issued by SEBI, and as may be pursuant to the Companies Act of 2013. These laws and regulations will be discussed to examine how they are helpful in supporting the objectives of transparency, governance, and ESG integration into the private investment process. The research will then proceed to undertake a legal comparison with global systems and determine how India’s regulatory regime governing private equity investment compare with international standards.

The methodology also will give a review of regulatory oversight of Alternate Investment Funds (AIFs), and its related effects on social impact investment and management. Hence, the paper seeks to make a legal and comparative analysis in relation to the “good governance” practices in India, and identify areas of strength and potential areas of enhancement.

LEGAL & REGULATORY FRAMEWORK GOVERNING GOOD GOVERNANCE PRACTICES IN INDIA:

Overview of Key Indian Laws & Regulations

The securities markets in India are mainly controlled by the SEBI that was constituted under the SEBI Act, 1992¹. SEBI as the market regulator for the Indian capital markets industry contributes greatly to the promotion of the transparent, efficient and fair capital markets in India, with a special emphasis on providing investors’ protection, maintaining equity and fairness, and promulgating effective governance standards. SEBI regulates many features of capital markets in India and exercises oversight over the issuance of IPOs, corporate governance, insider trading, and securities fraud, to name but a few areas². Its main mandate is to safeguard investor interests and also promote the efficiency of the market. With regard to this aspect, SEBI oversees private equity markets in relation to disclosures, pricing mechanisms, and the compliance regime that issuers have to meet in order to ensure that the public receives correct information.

¹ Securities and Exchange Board of India Act, 1992.

² Kamalnath, Akshaya. “A critical review of the development of capital markets in India.” Research Handbook on Global Capital Markets Law (2023): 386-399.

The Companies Act, 2013 directly affects corporate behavior when it comes to public offerings in India³. It requires that private businesses planning to list their securities in the public domain make disclosures to the public and provide adequate information to the potential investors. This part of this paper covers information regarding the company's operations, management, performance, risk and any event that may have taken place which may affect the company.

AIF Structures and Their Regulation by the SEBI

The Alternative Investment Fund (AIF) structure is an important vehicle that may be used to make private investments in India as described in SEBI (Alternative Investment Funds) Regulations, 2012. Pursuant to these regulations, an AIF is defined as a privately pooled investment fund that raises funds from domestic and international investors. These funds are managed with a specific investment formula that is intended to create benefits for the private investors. The regulations issued by SEBI are aimed at providing proper disclosures, appropriate regulation and compliance with the governing legal framework, and maintaining the standard of corporate governance that is applicable to all AIFs operating in India.

Governance and Reporting Requirements under the SEBI:

To ensure fair and efficient markets, the SEBI imposes various governance principles and legal requirements on AIFs. These requirements include:

³ Companies Act 2013 (No. 18 of 2013). For the sake of clarity and brevity, other elements of the Indian regulatory regime with respect to and as may impact private equity funds and investments in India, have been omitted. For references to certain regulations that may be applicable, please *see e.g.*, SEBI's Listing Obligations and Disclosure Requirements (LODR) Regulations, 2015 (last amended on July 10, 2024). <https://www.sebi.gov.in/legal/regulations/jul-2024/securities-and-exchange-board-of-india-listing-obligations-and-disclosure-requirements-regulations-2015-last-amended-on-july-10-2024-84817.html>. *See also, e.g.*, SEBI's issuance on 26 August 2009 of the Issue of Capital and Disclosure Requirements) Regulations, 2009 (ICDR Regulations), a general discussion of which and a checklist for SEBI ICDR regulations may be accessed at: <https://assets.kpmg.com/content/dam/kpmg/in/pdf/2017/03/SEBI-ICDR.pdf>.

- i. *Transparency and Disclosure*: AIFs are required to submit reports to investors at least annually, concerning the performance of the fund. There are special requirements for reports that are disclosed annually or more frequently. According to the SEBI, such reports must be filed at least within six months of the previous filing.
- ii. *Investor Protection*: The SEBI mandates that the prospectuses of the funds and other documents relating to funds such as the private placement memorandum should not conceal any material facts, but should give complete and accurate information to the investors.
- iii. *Valuation Norm*: These policies on valuation adopted by the SEBI require that AIFs conduct their business with accurate disclosures of the firm's fair value.
- iv. *Compliance Monitoring*: These funds are required to undergo periodic legal compliance review to confirm their compliance with the Indian laws on most legal, taxation, and other reporting requirements.
- v. *Governance Policies*: The SEBI bestows AIFs with robust recommendations such as independent advisory boards and policies involving conflict of interest.

(2) Corporate Structure and Flow of Funds:

i. Analysis of the Regulatory Status of AIFs with Respect to the IPO Process:

In accordance with SEBI (Alternative Investment Funds) Regulation, 2012. AIFs in India are pooled investment vehicles that raise money from the investors with an intention to invest it as per laid down in the investment management plan⁴. The IPO process that is in operation within the

⁴“A Guide to Foreign Investment in India.” 2024. *Deloitte* (July 11, 2024). <https://www.deloitte.com/lu/en/Industries/investment-management/blogs/a-guide-to-foreign-investment-in-india.html>. See also Sarangi, Gopal K. Resurgence of ESG investments in India: Toward a sustainable economy. No. 1284. ADBI Working Paper, 2021; Can, Who. 2016. “Alternate Investment Funds (AIFs)– Types, Benefits, Who Can Invest.” *Groww*, 2016, <https://groww.in/blog/all-about-alternate-investment-funds-aifs>.

Indian economy has been principally guided and regulated by policies and procedures issued and monitored by the SEBI. These laws and regulations have been put in place to ensure compliance with internationally accepted “best practices” governing private equity-financed companies as they intend to go public. These measures were adopted in order to protect investors.

The key steps involved in the IPO process include the following:

(a) *Regulatory Approvals*: The company needs to get regulatory approval from the SEBI before operating. This entails preparing and submitting a “Draft Red Herring Prospectus”(DRHP) that contains certain information concerning the company’s business, financial statements, directors and officers, and risks. The SEBI examines the document to check its response to the regulatory standards and requirements of legal disclosure demands⁵.

(b) *Underwriting*: Investment banks or other financial institutions buy shares as underwriters, and commit to purchasing or acquiring any excess shares, if there are any. This helps to guarantee the success of the IPO regardless of low public interest⁶.

(c) *Pricing*: IPO can be priced in two ways, *i.e.*, book building system or the fixed price system. With book-building, the final price is arrived at by adding the bids from possible institutional investors. Fixed pricing is a system in which the price is set by the company itself⁷.

⁵ Manu, K. S., and Chhavi Saini. “Valuation analysis of initial public offer (IPO): the case of India.” Paradigm 24, no. 1 (2020): 7-21. A “Draft Red Herring Prospectus” (DRHP) is a document that companies in India file with the SEBI when they plan to launch an Initial Public Offering (IPO). It is a preliminary registration document that provides investors with information about a company's business, financials, and risks. It is also known as an offer document.

⁶ *Ibid.*⁷

Ibid.

(d) *Listing*: After the shares are allocated for listing on the exchanges, investors are free to buy and sell the shares on the National Stock Exchange (NSE) or Bombay Stock Exchange (BSE)⁸. SEBI regulations seek to confirm that all companies' public floating shares are properly scrutinized, and that investors are given enough and accurate information of the float. The SEBI also regulates the manner in which listing companies may share corporate information. The SEBI also ensures that these companies follow post-listing disclosure regulations that require, for instance, that periodic financial information is duly provided to investors, a vital element in sustaining market confidence⁹.

(ii) Evaluation of the Current IPO Process:

The IPO process has also evolved at an international level to increase its efficiency and the quality of its compliance with the requirements for transparency and governance in Indian companies. However, there are some areas that need constant enhancement, particularly in the dynamics of addressing environmental, social, and governance (ESG) factors in the underlying Indian laws which require continuous improvement. Further, integrating ESG factors into the regulatory framework is also an important aspect of regulation. The SEBI has taken significant steps to increase the practice of transparency and other governance standards; however, the requirement for ESG integration in the IPO processes is rising globally, and will need to be addressed by Indian companies at present. IPO transparency has also been enhanced through the regulation in India, especially through the SEBI which has in the recent past required companies to file details of the company's financial position, risks, financials and proven plans, among others.

⁸ *Ibid.* ⁹
Ibid.

(iii) Incorporating ESG Factors into a Good Governance Framework:

The management of good governance, particularly of ESG factors, remains in its infancy globally. However, many firms are implementing ESG policies now in order to gain global investors. Further, India acting through the SEBI has made tremendous inroads in finalizing and implementing clear cut standards for mandatory ESG compliance for top listed companies in India. The process of creating clear regulations for and mandatory compliance with ESG performance-related reporting and disclosure has been an ongoing process beginning with the issuance of the Business Responsibility Report (BRR) by the SEBI in 2012. The BRR was a framework in India that required the top 100 listed companies to report on their ESG performance. The SEBI replaced the BRR with the Business Responsibility and Sustainability Reporting (BRSR) framework in 2021, which is a mandate for the top 1,000 listed companies in India to report on their ESG performance and demonstrate their commitment to responsible business practices.¹⁰ Further, these companies will be required to provide quantifiable metrics on sustainability-related factors, such as respect for human rights or environmental protection.¹¹

Compliance with the BRSR will be staggered beginning with the mandated compliance in 2024-2025 for the top 250 Indian companies by market capitalization. Ultimately, compliance with

¹⁰ See SEBI Master Circular for ESG Rating Providers, issued July 12, 2023, <https://www.sebi.gov.in/legal/master-circulars/jul-2023/master-circular-for-esg-rating-providers-erps-73856.html>. See also “Business Responsibility and Sustainability Report: What does it mean for the top 1,000 listed entities in India?” *Deloitte* (August 2023), <https://www2.deloitte.com/in/en/pages/finance/articles/business-responsibility-and-sustainability-report.html>. (The report may be downloaded from this site.) The BRSR requirements are based on the National Guidelines for Responsible Business Conduct (NGRBC).

¹¹ The Ministry of Corporate Affairs (MCA) of the Government of India issued the National Guidelines on Responsible Business Conduct (NGRBC) on March 15, 2019. The NGRBC were created by revising the National Voluntary Guidelines on the Social, Environmental and Economic Responsibilities of Business (NVGs), which were released in 2011. The NGRBC is designed to support the United Nations Guiding Principles on Business & Human Rights (UNGPs). See generally, Indian Institute of Corporate Affairs, https://iica.nic.in/sob_ngrb.aspx.

the BRSR will be required from the top 1,000 listed companies by 2027. While it is not expected that the IVCFs that are the focus of this paper will be within the top 1,000 listed companies in India, the BRSR nevertheless provides ESG compliance standards for IVCFs to review carefully and begin standardizing their business practices, reporting and monitoring of ESG factors going forward.

Challenges and Governance Enhancements

It is not surprising that IVCFs, face complex challenges related to implementing social investment initiatives while dealing with good governance issues. These challenges may be addressed by IVCFs by adopting international standards, including the ILPA Principles, discussed below, which help to set up a highly effective governance framework.

a) Corporate Best Practices:

A menu of best practices may be extracted from diverse sources, and the ILPA Guidelines, the IFC Performance Standards, and the Norfund Guidelines, all of which are good reference materials. The following analysis and recommendations set forth a course of action to address issues of corporate governance, transparency, and ESG disclosure and reporting in the IPO and private equity markets in India.

(1) ILPA Best Practices:

ILPA concepts are aimed at improving the quality of governance, organizational transparency, and the degree of alignment between LPs and GPs¹². Therefore, these standards creating clear fee and expense reporting systems should be adopted in India in order to eliminate the issues related to

¹² Lino, Marc, Liam Connolly, David Hoverman, Debra McCoy, Matthew Schey, and Samantha Anders. "Limited partners and private equity firms embrace ESG." *Bain & Company* (2022).

concealing the extra charges that may damage the faith of investors. As with reasonable profit-sharing structures, the distribution of profits is also done fairly, which minimizes conflicts of interest¹³. One potential with firms in India is to establish Limited Partner Advisory Committees (LPACs) which are prevalent in the global markets and can be effective for Indian firms. LPACs are formed for the purpose of advising the General Partner (GP) on specific issues during the lifetime of a fund, including conflicts of interest and material changes to the governing documents of the fund where the Limited Partner's (LP's) consents or approvals are required.

Thus, through the operation of the LPACs, investors may directly engage in significant processes that take place and improve accountability and corporate governance throughout the investment decision-making process.

(2) IFC Performance Standards:

The IFC Performance Standards provide a clear guideline of how to mitigate environmental and social risks. In the case of Indian firms, especially those planning for IPOs, environmental and social risk management which pays for physical environment and social risks, is vital for establishing and maintaining social sustainable businesses¹⁴. Social sustainable enterprises are businesses that prioritize social goals while remaining financially sustainable. Other aspects of the IFC standards include stakeholder engagement and community consultation, and these should be the focal points of Indian companies to ensure that consultation and engagement are done effectively and sustainably. ESG reports and impact estimates should be performed routinely and enhance corporate transparency and accountability so that businesses follow the law and meet the

¹³ *Ibid.*

¹⁴ "Impact Investing at IFC. <https://www.ifc.org/en/our-impact/impact-investing-at-ifc>.

expectations of their investors. The aforementioned standards may be a reference point for Indian companies with the purpose of establishing and requiring ESG compliance for themselves both nationally and internationally.

(3) Norfund Guidelines:

The guidelines provided by the Norfund, the Norwegian Investment Fund for Developing Countries, speak equally of responsibilities with regard to business conduct and sustainable value creation¹⁵. In the context of India, these guidelines may be implemented by building up the capacity and corporate governance of the companies in which investment is made, in other words, by the IVCF's investee companies. This approach contributes to the fact that businesses not only meet ESG requirements but also serve the further socio-economic advancement of the downstream users of the private financing in the regions these businesses have invested in. Norfund's emphasis on sustainable development has similarities to the visions of many Indian private equity firms, especially those operating in sectors like renewable energy, healthcare, and education¹⁶.

As a result, incorporating elements of ILPA, IFC, and Norfund will help improve the existing governance and ESG structures of the Indian companies and, as a consequence, turn them into more appealing investment propositions on the global playing field. These good governance practices not only yield developments that enhance current governance systems, but they also lay the foundation for sustainable development keyed into regional legislation and international standards.

¹⁵ "Operating Principles for Impact Management – Norfund." 2024. *Norfund* (June 11, 2024); see <https://www.norfund.no/ifc-operating-principles-for-impact-management/>.

¹⁶ *Ibid.*

b) Applying the ILPA Principles to Enhance Corporate Governance:

Based on my review of the foregoing ILPA, IFC and Norfund “best practices,” ILPA’s guidance is best suited to INVCs for the reasons set forth below. At the outset, the ILPA Principles are an effective instrument in improving corporate governance at all stages of investment. They present the common guidelines regarding governance and interests’ leveling of limited partners (LPs) and general partners (GPs), namely through information disclosures, the fair share of gains, and sustainable value generation¹⁷. These principles are particularly valuable because they provide a standardized framework that ensures transparency, accountability, and alignment of interests, fostering trust and minimizing conflicts between LPs and GPs. These principles are most effective for IVCFs and similar PE firms to address governance issues at various stages of the fund’s life cycle.

(1) Seed Round: Phase One (Seed through Series A round)

In the seed stage, it is very important to define the rights and obligations of founders, initial investors, and venture capitalists concerning the governance framework. At this stage, ILPA principles may help develop governance structures that will safeguard initial investments and align the founders with early investors¹⁸. Any major corporate governance structures must include and meet the expectations of shareholder agreements. This will allow the founders to remain in charge of critical business decisions while taking into account the expectations and input of the early investors. This will permit early governance structures to create and support “trust networks” with early and potential investors, the very actors upon whom future rounds of investments will depend.

¹⁷ “Operating Principles for Impact Management– Norfund.” 2024. Norfund. June 11, 2024. See <https://www.norfund.no/ifc-operating-principles-for-impact-management/>.

¹⁸ *Ibid.*

The engagement of IVCFs with an investee company at the seed round involves cooperating with startups to define its ESG objectives and implement them with a focus on socially oriented businesses. However, the governance structures at this stage should also take into account the ethical and social responsibilities of the chosen business model that align with long-term ESG outcomes.

(2) Growth Stage: (Phase 2: Series B-C rounds)

During the growth stage, there is usually a change of responsibilities as more corporate entities, like private equities and institutions, invest in the company, to wit, the IVCF's investee company. It is argued that at this stage there is a need to change governance structures to accommodate emerging stakeholders¹⁹. According to the ILPA best practices, this stage encompasses making an effective communication and a decision-making plan on how to include new investors. This must be done carefully so that it does not derail the prior strategic plans made in the previous stages of funding and investor participation in governance questions. At this stage, governance should be concentrated on such measures as openness and power-sharing among the stakeholders. Like many other private equity firms that have been established in the recent past, an IVCF must be careful to effectively balance the need for governance structures that are robust enough to support growth along with the need to respond to change when increased capital inflows impact stakeholders' needs, interests, and power-sharing.

(3) Pre-IPO Stage: (Phase 3: Expansion; Series D, if there is one, through the Issuance of IPO)

The pre-IPO stage is a point when firms plan their public offering, and governance needs to align with applicable regulations and market demand. According to the principles of the ILPA, it is

¹⁹ Stowell, David P., "An introduction to investment banks, hedge funds, and private equity.," *Academic Press*, 2010.

important to focus on the convergence of the interests of investors and managers, particularly in those companies that are moving from the private sector to a publicly listed one²⁰. Management structures at this stage require making decisions with a view to public accountability, especially on such issues as pricing and risk disclosure.

At this stage, for IVCs and other private equity firms, organizational governance changes are usually made to address the new challenges associated with a possible public offering. This entails guaranteeing that all the reported ESG and other relevant policies are complied with and that the governance systems are capable of passing through the scrutiny of the public market (as well as the SEBI), including making meaningful due diligence reviews, and complying with listing requirements on stock exchanges, including the BSE and/or the NSE.

(4) IPO Stage: (Phase 4: Exit through the Issuance of an IPO)

At the IPO stage, the transition in responsibility takes place among various stakeholders, such as boards of directors, shareholders, and regulators. According to the ILPA principles, there are ways in which to handle such changes in a way so that governance does not deteriorate in the middle of this process. Priority areas include the dynamic combination of the company's board of directors, addressing public markets outreach and related needs, having a clear and fair governance system in place, and encouraging shareholder engagement in support of sustainable goals²¹. Implementing the ILPA principles specifically in the IPO phase where an IVC going through a public listing exercise highlights the need for explicit and transparent good governance practices. It also entails

²⁰ "Operating Principles for Impact Management– Norfund." 2024. Norfund. June 11, 2024. <https://www.norfund.no/ifc-operating-principles-for-impact-management/>.

²¹ "Operating Principles for Impact Management – Norfund." 2024. Norfund. June 11, 2024. <https://www.norfund.no/ifc-operating-principles-for-impact-management/>.

the protection of ESG strategies and policies from getting distorted by the operational requirements of the public market interface. It is critical in this phase to remain true to the espoused ethical and social responsibility principles that defined the initial investment phase.

COMPARATIVE ANALYSIS AND BEST PRACTICES IN INDIA AND GLOBAL CONTEXTS:

Comparative Overview:

In light of the rapidly emerging ESG standards being applied to the equity investment market in India, the Indian IPO market has its pros and cons. India's own IPO process is mainly governed by the SEBI, and strongly resembles the capital market regulations systems such as that of the Securities and Exchange Commission (SEC) of the United States, and the Financial Conduct Authority (FCA) in the United Kingdom. As a result, the SEBI already reflects most of these international standards of corporate governance, specifically in the arenas of transparency, governance, and investor protection. However, there are certain nuanced variations, particularly where the SEBI departs from these norms in the implementation of ESG standards.

The integration of ESG standards in India through regulatory requirements, discussed above, is beginning to mirror, but is still relatively behind, sophisticated securities markets in Europe and the United States. In India, the SEBI's Business Responsibility and Sustainability Reporting (BRSR) specifies mandatory disclosures relevant to the environmental and social challenges for private companies with substantial market capitalization. These mandatory disclosures include reporting on greenhouse gas emissions, water and waste management, and social impact assessments. In contrast, the EU's Sustainable Finance Disclosure Regulation

(SFDR), which was introduced in 2019 and came into effect on March 10, 2021, is part of the European Commission's Action Plan on Sustainable Finance²². It applies to EU market participants with over 500 employees including institutional investors, venture capital funds, alternative investment funds who are required to list a number of ESG-related disclosures on their websites.²³ However, the Commission is currently reviewing the SFDR with a view to assess its role in preventing "green-washing," and is still in its consultative stage as of May 3, 2024²⁴

Thus, a key contrast with the Indian BRSR regulatory regime is that it is directed at the top 1,000 private companies to be listed by FY 2027, whereas, the SFDR regulates PEs in the European market with more than 500 employees. Indeed, a recent study found that the SFDR had the most comprehensive framework for the financial market participants. Whereas the BRSR framework stops at the disclosures related to the business itself, the SFDR goes a step further by including the indicators related to the investee companies.²⁵

Potential and actual legal and regulatory constraints to innovation may have major impacts on business and other specific industries that either pose environmental or social risks or that are otherwise subject to significant flexibility regulation. ESG compliance costs are sometimes a problem for such companies, and mismatched global and local standards make it difficult to build coherent strategies around ESG factors and considerations.

²² *Ibid*

²³ See "Sustainability-related disclosure in the financial services sector," *European Comm'n (2024)*, https://finance.ec.europa.eu/sustainable-finance/disclosures/sustainability-related-disclosure-financial-services-sector_en. See generally, "What is the Sustainable Finance Disclosure Regulation (SFDR)?" *SWEEP*, (June 17, 2024), <https://www.sweep.net/insights/what-is-the-sustainable-finance-disclosure-regulation-sfdr>.

²⁴ *Ibid*.

²⁵ See Amit Garg, *et al.*, "Comparative analysis of sustainability related disclosure frameworks: SFDR, IFC PS, and BRSR," *Indian Institute of Management, Ahmedabad*, W. P. No. 2024-10-01 (October 2024).

Lessons Learned from Global Practices:

In light of the discussion above, it is important to apply international standards to the Indian context as a means of advancing ESG integration in equity investments by PE firms. These standards are set mostly by international investors who use the internet as their main communication and business tool. As an example, foreign institutional investors (FIIs) like pension funds and sovereign wealth funds set very high ESG standards for companies in which they invest, including companies in India²⁶. Indeed, the actions of India's competitors introduced global ESG benchmarks onto the Indian market, thus forcing Indian domestic companies to meet international standards.

The Limited Partner Advisory Committees (LPACs), for instance, have become much more involved in decision-making processes and promoting improved governance accountability. LPACs are common in many structures of international private equity, and provide mechanisms for expression of concern on governance and ESG issues which Indian firms are gradually adopting.²⁷ Moreover, the global trend of focusing on fee structures and performance reporting has affected the Indian regulators who are now pressing for more concrete disclosures, particularly in IPO documents. Applying these global standards is also useful to Indian firms in enhancing their understanding of ESG risks, integrating better with international investors, and promoting sustainable development in India as well as globally.

²⁶ Matos, Pedro. "ESG and responsible institutional investing around the world: A critical review," (2020); available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3668998.

²⁷ Singhania, Monica, and Neha Saini. "Institutional framework of ESG disclosures: comparative analysis of developed and developing countries." *Journal of Sustainable Finance & Investment*, 13, no. 1 (2023): 516-559.

CONCLUSION:

(a) Summary of Key Findings:

This paper has explored the complex IPOs, ESG, and corporate good governance issues in India with an overview of how these issues fit into a more global perspective. IPOs act as a critical and growing source of funding. Moreover, India's regulatory mechanisms, set forth in the SEBI Act, the Companies Act 2013 of India, and other applicable and relevant legislation, protect both domestic and foreign private investors, and follow international standards. ESG factors are gradually being incorporated into investment processes, which is widely supported by domestic and overseas investors.

The governance practices set forth in the global benchmark practices of the ILPA along with IFC standards, all provide critical guidance to improve the worldwide market demand to make sustainable investments and to promote sustainable value creation, as discussed above.

(b) Future Directions:

As with many other countries, India's regulation and ESG environments continue to develop, but India may wish to consider further legal and policy initiatives for greater alignment with current ESG norms in more mature global markets such as Europe and the U.S. Several forward-looking solutions should be considered in this context. First, ensuring the greater implementation of appropriate ESG rules and extending the SEBI's control over international private equity firms incorporated under foreign laws are a good starting point.

Additionally, enforcing more stringent ESG reporting standards may help improve ESG standards in India. Also, specific to India, there is much that can be learned from global best practice frameworks such as ILPA principles and IFC performance standards which call for more

governance enhancement, especially in areas of transparency, stakeholders' participation, and community engagement in all stages of investment and growth. Following best practices from around the world, India is poised to become the leader in integrating ESG, and other "good governance" practices, into its emerging private investment environment.

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ANNEX

Private Equity and ESG Integration

a) The Importance of ESG in Private Equity:

Environmental, social, and governance (ESG) considerations for companies' behavior have become critical measures, especially in private equity. These standards cover everything from a company's environmental responsibility to its impact on workers, local communities, and governance, which refers to behaviors such as disclosure, corporate integrity, and shareholders' rights. Rising interest in responsible investment has placed pressure on private equity firms internationally to submit to sustainable work plans and models that incorporate ESG into investment because investors do not only look for profits but also for change therein.

b) Legal and Ethical Considerations:

ESG disclosure has been recently included by the SEBI through Business Responsibility and Sustainability Reporting (BRSR) for listed companies, but it is not uniformly applicable to private equity funds²⁸, particularly those that are not among the top 1,000 listed companies. Insofar as BRSR mandatory requirements may not strictly apply to For IVCFs that are the focus of the paper who fail to register in the top 1,000 companies by FY 2027, as such, private equity firms are not strictly mandated to adhere to BRSR's disclosures at this time. Nevertheless, these private equity firms have an opportunity contextualize their ESG compliance, taking into account the BRSR, but also considering other global ESG standards that its investors may already be expected to comply with, including the SFDR.

²⁸ Srivastava, Ashish Kumar. "ESG Framework: Balancing, Profit, Public & Planet," *CMR Univ. J. Contemp. Legal Aff.* 5 (2023): 101.

A second consideration that may be incorporated into an IVCF's ESG approach is to review and incorporate, as may be appropriate, the Institutional Limited Partners Association (ILPA) Principles which provide guidance on private equity firms' ESG platform. Based on ILPA guidelines, certain sectors, such as equipment leasing, are most appropriate for ESG-related regulation as most assets managed in this sector require long-term management and have impacts on the environment. In the global environment, PE firms that subscribe to ILPA standards are expected to lead by example in terms of their transparency and governance practices in rolling out ESG management throughout their portfolios²⁹. This means ascertaining or exercising careful inquiry not only on the financial viability of projects but also on the various environmental and social responsibilities before committing to a project.

Unlike the European Union's Sustainable Finance Disclosure Regulation (SFDR), India does not currently require similar stringent ESG compliance³⁰. India's ESG disclosure regulations, led by the SEBI's Business Responsibility and Sustainability Reporting (BRSR) is still not as exhaustive as the European system and the Sustainable Finance Disclosure Regulation (SFDR). While the SFDR has raised the bar in terms of both the stringency and detail of disclosures requested on ESG factors for financial market participants, India's BRSR is less burdensome in terms of the scope of its requirements and in the number and type of businesses to which they apply, as the BRSR primarily targets larger companies listed on the Indian stock exchange. The absence of similar rigid regulatory standards (as found in the SFDR) in India may be attributed to

²⁹ Ivashina, Victoria. "Private equity financing." *Handbook of the Economics of Corporate Finance: Private Equity and Entrepreneurial Finance* (2023): 139.

³⁰ Tsikata, Bright Kojo, Lordina Amoah, and Joshua Ogwal. "Regulation of sustainable and responsible investment in developing countries." *In Sustainable and Responsible Investment in Developing Markets*, pp. 397-410. Edward Elgar Publishing, 2023.

the gaps in regulation, most particularly with respect to private entities including the private equity funds that are smaller in size, even if these funds are listed on local stock exchanges.

However, India, like other countries in the Global South, has increasingly been compelled by global investors to adopt good governance practices of its own accord. Accordingly, Indian regulators and the business community may wish to integrate the principles of ILPA into investment strategies in India, and require that its investments meet the international compliance standards for ESG. Even if IVCFs use an AIF structure for example, and have a market capitalization of less than the top 1,000 listed companies in India, the organization's ESG adherence and management can be seen in two ways. On the one hand, it gives the firm the opportunity to flexibly implement ESG approaches that coincide with its overall investment approach in cases where the firm is not bound by the local legislation such as the BRSR. On the other hand, this also poses problems such as the lack of external regulation concerning ESG reporting for such IVCFs. Therefore, these IVCs should be encouraged to set up stringent *internal regulations* to ensure that its business and its impact in India satisfy the global standards set for ESG compliance. This means that IVCFs must maintain its integrity coupled with its accountability when reporting the ESG impacts of its investee firm to domestic and global investors.

(c) Lessons Learned in Creating an ESG Policy:

The IVCF's ESG policy should stem from its sustainable investing business principles as well as community welfare considerations and sound ethical standards. The assumption within this approach is that financial performance should come with the consideration of social responsibility, especially in developing countries such as India. This policy focuses on funding only those

organizations, companies, or funds that are financially sound and socially and globally responsible. This approach assists IVCFs to guarantee that all their portfolio companies are solving other common societal problems like tackling inequality and advancement of modern stability and economic growth.

The firm's vision of good business ethics encompasses accountability and disclosure, supply chain and procurement, work remuneration, and organizational governance in relation to the rights of various players. Likewise, IVCFs should be encouraged to adopt a robust ESG policy in which it espouses the belief of community enhancement to foster sustainable value within the targeted communities of the invested portfolio firms. This is especially critical in the IVCF's focus sectors, which comprise industries that provide and/or seek to solve societal problems such as extending credit facilities or providing health care facilities to vulnerable or less privileged customers³¹.

d) Comparison with International Benchmarks

The ESG policy of any prospective IVCF should, in principle, correspond with several global best practices, such as IFC Performance Standards, United Nations Principles for Responsible Investment (UNPRI), and ILPA principles. These frameworks offer internationally accredited frameworks of how ESG should be implemented in private equity, aspects such as environmental management and social issues, governance structure, among others. For instance, the IFC Performance Standards that focus on environmental and social risk assessment obligate companies

³¹ Ibid

to manage their adverse effects on communities and the environment³². The ESG policy followed by IVCFs is designed to ensure that it only invests in projects that are both ethical and sustainable.

In its implementation of the UNPRI, IVCFs should agree to address ESG factors in the investment management processes. This means that rather than ESG factors simply being an additional component of the decision-making process, they are an integral part of the firm's strategic tools³³. Further, the ILPA Principles define governance practices that may be implemented by an IVCF, including establishing investors and managers in synergistic relationships, ensuring proper profit allocation, and supporting the active participation of advisory committees.

e) Regulatory Approaches

Regardless of whether the IVCF operates as an AIF, it may adopt many of the regulatory practices that SEBI is developing for sustainable investing. Most importantly, the SEBI-mandated Business Responsibility and Sustainability Reporting (BRSR) applies to listed Indian companies with significant market capitalization who are required to provide quantifiable metrics on sustainability-related factors, such as respect for human rights or environmental protection.

Applying these standards to a prospective (and smaller) IVCF demonstrates that, despite operating in India which may not have many codified laws applicable to smaller PEs, these firms nevertheless are willing to be transparent and accountable, and be fully committed to taking that

³² "Impact Investing at IFC." *IFC*, <https://www.ifc.org/en/our-impact/impact-investing-at-ifc>.

³³ Young-Ferris, Anna, and John Roberts. "Looking for something that isn't there': a case study of an early attempt at ESG integration in investment decision making." *European Accounting Review* 32, no. 3 (2023): 717-744.

approach. This approach to governance and ESG standards guarantees that IVCF's investments conform to global and local standards, which makes it a good and responsible player in the global private equity space.