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Insight

Analysis of Recent Developments in Indian Corporate Law

Foreword

Welcome to this issue of *Insight*.

In this issue of *Insight*, as the lead article, we have covered the recent changes made by SEBI to the regulations governing schemes of arrangement involving listed companies. This issue also covers the recent regulatory changes pertaining to the listing of Real Estate Investment Trusts (REITs) and Infrastructure Investment Trusts (InvITs).

Apart from the above, we have also covered the key amendments and notifications issued by the Ministry of Corporate Affairs, the Reserve Bank of India and SEBI, in the last quarter.

Any feedback and suggestions would be valuable in our pursuit to constantly improve *Insight* and ensure its continued success amongst readers. Please feel free to send any feedback, suggestions or comments to insight@cyrilshroff.com.

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SEBI ISSUES REVISED CIRCULAR ON SCHEMES OF ARRANGEMENT INVOLVING LISTED ENTITIES

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The Securities and Exchange Board of India ("**SEBI**"), at its board meeting held on January 14, 2017 approved certain revisions to the regulatory framework applicable to schemes of arrangement by listed companies. The revisions were considered necessary to incorporate additional safeguards in the regulatory regime to prevent the misuse through schemes designed to bypass regulatory requirements and prejudice the rights of public shareholders, which were hitherto being addressed by SEBI on a case by case basis while commenting on the relevant schemes of arrangement. To bring about consistency and to streamline the regulatory framework, the revisions were codified by an amendment to the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009 ("**ICDR**") as also SEBI's circular dated March 10, 2017 ("**Scheme Circular**"). We have set out below the key changes brought about by the amendment to the ICDR and the Scheme Circular.

Applicability

- The Scheme Circular is only applicable to schemes submitted to the stock exchanges after March 10, 2017. The SEBI circular dated November 30, 2015 ("**2015 Circular**") will continue to govern schemes filed with the stock exchanges on or prior to March 10, 2017.

- Schemes of arrangement which provide solely for the merger of a wholly owned subsidiary of a listed company with its parent are exempt from applicability of the Scheme Circular, since no material regulatory concerns are likely to arise in case of such schemes. Such schemes, whilst not subject to SEBI's review and approval, are required to be filed with the stock exchanges for the purposes of disclosures and dissemination on the stock exchange's websites. SEBI's relaxation of the review process for such schemes is in keeping with the general trend towards SEBI's simplification of the regulatory regime for transactions between wholly owned subsidiaries and its parent, such as the exemptions provided from compliance with certain requirements for related party transactions.

Key changes

- *Preferential issues as part of schemes and adherence to pricing guidelines*: Previously, issuances of shares made pursuant to schemes of arrangement were exempt from the application of Chapter VII of the ICDR, which, *inter alia,* prescribes pricing norms for preferential allotments based on a formula which incorporates the average price of shares of the listed company for a certain period prior to an identified 'relevant date'. To prevent the exemption from being used to allot shares to select groups of persons or promoters at a discounted price, the ICDR were amended with effect from February 15, 2017 to specify that pricing guidelines set out in Chapter VII of ICDR will be applicable to allotment of shares pursuant to a scheme (i) only to a select group of shareholders; or (ii) to the shareholders of unlisted companies. The Scheme Circular reiterates that listed companies are required to comply with the pricing guidelines under the ICDR for the circumstances mentioned above. While there was some ambiguity on the 'relevant date' to be considered for computing the applicable price, SEBI has subsequently clarified by its circular dated March 23, 2017 that the 'relevant date' for computing the price will be the date of the board meeting at which the scheme is approved.

  In relation to allotment of shares to a select group of shareholders as set out in (i) above, assuming that the requirement relates to preferential allotments which would have been required to comply with the requirements under the ICDR had it been made outside of a scheme, the change achieves the intention of providing a minimum price (equivalent to the regulatory floor price had such issuance been made outside a

scheme) at which such shares can be allotted, thus safeguarding against issuances below such floor price.

It is relevant to note that judicial precedent has established that a variety of valuation methods are required to be followed by experts to establish that the share exchange ratio in a scheme of merger is fair and reasonable. It is therefore unclear how this will interplay with the requirement to comply with the pricing guidelines set out in Chapter VII of ICDR.

- *Compliance report*: Listed companies are now required to submit a detailed compliance report in a prescribed format to the stock exchanges prior to filing the scheme with the National Company Law Tribunal ("**NCLT**"). The compliance report must be signed by the company secretary, the chief financial officer and the managing director of the company and confirm compliance with various regulatory requirements and accounting standards applicable to a scheme. SEBI's intention in introducing this requirement is to promote self-regulation by companies and to expedite the processing of draft schemes by SEBI and the stock exchanges by streamlining the documentary requirements which were earlier independently imposed by the stock exchanges.

- *Public Shareholder approval:* The Scheme Circular has added the following two circumstances where a scheme would require approval of the majority of public shareholders: (i) a scheme involving the merger of an unlisted entity with a listed entity resulting in reduction in the voting shares of the pre-scheme public shareholders of listed entity by more than 5% of total capital of the merged entity; and (ii) a scheme involving a transfer of the whole or substantially the whole of the undertaking of the listed entity where the consideration is not in the form of listed equity shares.

  These measures are intended to protect the interests of minority shareholders where they are either significantly diluted as a result of an amalgamation involving an unlisted entity or where the listed company seeks to transfer a significant part of its business without offering equivalent liquid equity shares to its shareholders. The new requirement to seek public shareholder approval when the consideration is not in the form of listed shares is consistent with SEBI's past views (albeit previously not part of the regulations) that schemes should not be used as a mode for 'back door de-listing'.

  In terms of procedure for public shareholder approval, listed companies are now required to mandatorily facilitate voting by public shareholders by way of e-voting unlike the 2015 Circular which mandated postal ballot as well as e-voting.

- *SEBI approval for change to scheme after filing:* Specific prior written consent of SEBI is now required if the parties to a scheme seek to make any changes to the draft scheme after filing the scheme with the stock exchanges. An exception has been provided for changes mandated by regulators, authorities, the court or tribunal. This amendment is to preclude companies from rendering the regulator's scrutiny of a scheme ineffective by making changes to the scheme after the date of SEBI or stock exchange approval. However, no specific time frame has been prescribed for SEBI to approve or reject revisions to the scheme. The amendment is an incremental compliance requirement given that schemes are subject to final approval by SEBI after sanction by the High Courts/NCLT and SEBI may withhold its approval if it did not agree with any changes to the scheme. In practice, the approval of SEBI is typically sought for any material modification and minor modifications have been notified to SEBI. However, all minor modifications may now have to be approved by SEBI pursuant to this change.

- *Conditions for schemes involving unlisted entities:* In line with SEBI's objective of preventing misuse of schemes, SEBI has prescribed additional conditions relating to schemes involving unlisted companies. These changes seek to place certain restrictions on schemes which allow shareholders of an unlisted entity to receive listed shares

pursuant to a scheme without an initial public offering. SEBI has also enhanced the disclosure requirements for such schemes to equip shareholders of listed companies with sufficient information while voting. The following conditions are applicable to schemes between listed and unlisted entities:

(i) While seeking approval of shareholders for a scheme involving an unlisted entity, a listed entity is required to set out information pertaining to the unlisted entity in the explanatory statement accompanying the resolution in the form prescribed for an abridged prospectus in the ICDR. The accuracy and adequacy of these disclosures are required to be verified by a SEBI registered merchant banker.

The abridged prospectus containing information regarding unlisted entities now also forms part of the list of documents to be submitted to the stock exchanges prior to the filing of a scheme with the NCLT.

(ii) The percentage of shareholding of pre-scheme public shareholders of the listed entity and the qualified institutional shareholders ("**QIB**") of the unlisted entity in the post scheme shareholding pattern of the 'merged' company should not be less than 25%. The change indicates that SEBI would not treat non-QIB shareholders as public shareholders.

(iii) Unlisted entities can merge with a listed entity only if such listed entity is listed on a stock exchange having nationwide terminals. This is consistent with the trend towards de-recognition of regional stock exchanges by SEBI.

- *Additional conditions for seeking relaxation under Rule 19(7) of Securities Contracts (Regulations) Rules, 1957* ("**SCRR**"): Apart from conditions set out in the 2015 Circular for seeking relaxation from the requirements of making an initial public offer when an entity seeks to list its shares pursuant to a scheme, the Scheme Circular prescribes lock-in restrictions where a scheme involves the hiving-off of a division from a listed entity into an unlisted entity seeking listing under the scheme. As a matter of practice, SEBI has often imposed lock-in requirements upon shareholders of unlisted entities which are proposed to be listed pursuant to a scheme under the aforesaid relaxation, and these lock-in restrictions have now been codified in the Scheme Circular as follows:

  (i) shares held by promoters up to 20% of the post-merger paid-up capital of the unlisted issuer will be locked-in for 3 years from the date of listing of the shares of the unlisted issuer; and

  (ii) the remaining shares will be locked-in for a period of 1 year from the date of listing of the shares of the unlisted issuer.

  No lock-in is prescribed where the post scheme shareholding pattern of the unlisted entity is identical to the shareholding pattern of the listed entity.

  SEBI's objective in introducing these lock-in requirements is to align certain restrictions on share transfers applicable to an initial public offer under the ICDR to shares that are listed pursuant to the Scheme Circular. However, relaxations from the lock-in requirements for shares issued under employee stock option schemes and shares issued to registered venture capital and foreign venture capital investors under the ICDR are not available to shares listed pursuant to the Scheme Circular.

- *Payment of fees to SEBI:* Similar to the filing fee payable for draft offer documents and draft open offer documents, SEBI has now prescribed filing fee for schemes of arrangements as well. Upon sanction of the scheme, each listed entity which is party to a scheme is required to pay to SEBI a fee of 0.1% of the paid-up capital of the listed/ transferee/ resultant company, whichever is higher, subject to a cap of Rs. 500,000.

This fee is in addition to the processing fees payable by companies to the stock exchanges.

Other requirements in relation to (i) choosing a designated stock exchange; (ii) obtaining a valuation report form an independent chartered accountant; (iii) obtaining a fairness opinion from a merchant banker on valuation of assets or shares done by the valuer for the listed entity and unlisted company; (iv) obtaining an auditor's certificate on accounting treatment contained in the scheme; (v) submitting the 'report on complaints' which contains details of complaints/comments received by the company on the draft scheme; (vi) disclosing the draft scheme and observation letter from the stock exchanges on the website of the company; (vii) submitting documents to the stock exchanges after the scheme is approved by the NCLT; and (viii) conditions for seeking relaxation under Rule 19(7) of the SCRR, remain unchanged from the 2015 Circular.

Listed companies proposing a scheme of arrangement with other listed or unlisted companies will need to be mindful of compliance with the requirements set out in the provisions of the Scheme Circular.

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LISTING OF REITS AND INVITS: BETTER LATE THAN NEVER

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The legal framework for listing of infrastructure investment trusts ("**InvIT**") and real estate investment trusts ("**REIT**") was notified by SEBI on September 26, 2014, under the chairmanship of Mr. U. K. Sinha. However, absence of listing of an InvIT or REIT after almost 2 years of notification of the SEBI (InvIT) Regulations, 2014 (the "**InvIT Regulations**") and SEBI (REIT) Regulations, 2014 (the "**REIT Regulations**") was a regret that the former SEBI chairman Mr. U. K. Sinha had mentioned prior to his stepping down and is also a question that has vexed various stakeholders.

Whilst it may seem that there has been an inordinate delay in achieving even one InvIT or REIT listing, the reasons for that are not far to seek. InvITs and REITs are complex products and a successful listing requires co-ordination amongst many governmental and regulatory authorities and there was a need to streamline the applicable regulations to facilitate listing.

Pursuant to a consultative process with various stakeholders, including prospective issuers, SEBI had amended the InvIT Regulations and the REIT Regulations, which were notified on November 30, 2016 (the "**November Amendments**"). Some of the important facilitative changes resulting from these amendments are summarized below:

- *Rationalisation of the definition of 'Associates'* - The definition has now been broadly aligned with the Companies Act, 2013 (the "**2013 Act**"). It is important to highlight two important categories of entities which have been removed from the definition – they are: (i) the related parties of an InvIT/ REIT, and (ii) entities where a person holds 15% or more equity share capital or partnership interest. This eases compliance with the disclosure requirements in terms of both, the application for registration of InvIT/ REIT with SEBI and the offer documents.

- *Two-tier structure* - Previously, the InvIT Regulations and the REIT Regulations stipulated that the special purpose vehicles ("**SPVs**") should be directly held by the InvIT/ REIT and any intermediate holding company structure was not allowed. With the November Amendments, two-tier holding structure for SPVs has been allowed. As companies in both infrastructure sector and real estate sector are often organized in multi-layered structures, this amendment reduces pre-IPO restructuring and attendant regulatory compliances and costs.

- *Subordinate units to Sponsors* – Prior to the November Amendments, different classes of units were not allowed under any scenario. Pursuant to the November Amendments, subordinate units with inferior voting or other rights can be issued only to the Sponsors or their associates. This is an important commercial change, which allows the Sponsors to forego distributions if there are any assets which have residual execution risk or where such assets do not have a long track record of operations and revenue generation. In such cases, the Sponsors can forego distributions on their unitholding till the relevant assets stabilize and those amounts can be distributed to other unitholders, providing a boost to their yields and earnings per unit.

- *Power to relax strict enforcement of regulations* – This power of SEBI was conspicuously absent from both the InvIT Regulations and the REIT Regulations. Considering that the legal framework pertaining to InvITs and REITs is in its infancy, they would be governed by a variety of laws with limited jurisprudence, it was very important to provide this power to SEBI to address any teething problems.

In addition to the above, the minimum Sponsor unitholding requirements (locked-in for 3 years from listing) for InvITs has been reduced from 25% to 15%, subject to the Sponsor or its associate being the Project Manager for a period of 3 years, unless changed at unitholders' initiative. Additionally, for REITs, the category of assets that can constitute the asset portfolio of REITs has been broadened to include: (i) hotels, hospitals and convention centers forming part of composite real estate projects (irrespective of whether they are income or rent generating), and (ii) common infrastructure for composite real estate projects, industrial parks and special economic zones. Concomitantly, the requirement for revenues from rental, leasing and letting or activities incidental to that has been reduced from 75% to 51%.

During the last year, SEBI had also notified the legal framework for various ancillary activities related to listing of InvITs and REITs, such as guidelines for undertaking a public offer, and requirements related to disclosure of financial information in offer documents and other continuous disclosure requirements.

Despite the immense effort put in by SEBI to facilitate listing of units of InvITs and REITs, there were some actions pending on the part of other regulatory authorities which were absolutely critical. The most important out of these was the ability of various domestic institutional investors to subscribe to units of InvITs and REITs.

In February, 2017, SEBI notified the governing provisions for investment by domestic mutual funds in InvITs and REITs (particulars of which are covered separately in this issue of *Insight*). This was followed by a notification issued by the Insurance Regulatory and Development Authority of India ("**IRDAI**") in March, 2017, allowing insurance companies to invest in units of InvITs and REITs, subject to certain specified investment conditions. Lastly, the Reserve Bank of India has, in its statement on developmental and regulatory policies, proposed to allow banks to invest in the units of InvITs and REITs, under their capital markets exposure, within the umbrella limit of 20% of net owned funds applicable to investment by the banks in equities, equity-linked mutual funds and venture capital funds.

Even though the operational guidelines would be issued in end-May, 2017, this announcement, at the least, lays to rest debate in some industry circles on whether investment by banks in the units of InvITs and REITs would be considered capital markets exposure or lending exposure. In addition to these developments, other stakeholders involved in the listing of units of InvITs and REITs (such as concessioning authorities and lenders) have also become comfortable with InvIT and REIT structures after extensive discussions. Their consents are a pre-requisite for transfer of SPVs/ assets by the Sponsors to InvITs/ REITs and some of these consents have been granted or are in the process of being granted.

In view of the above developments, the listing of InvITs seems distinctly achievable in next couple of months, especially since three issuers have filed draft offer documents with SEBI and one has received SEBI's final observations. Additionally, one of the InvITs is taking the private placement route to listing and based on publicly available information progressing towards listing at a steady pace. A REIT listing seems a little far away at this point, considering that only one application for registration of a REIT has been filed with SEBI.

There are also certain regulatory issues, which if resolved would provide further impetus to an InvIT or a REIT listing in the near future. There continues to be speculation over whether the units of InvITs/ REITs are '*security*' under the Securities Contracts (Regulation) Act, 1956. Also, whilst pension and provident funds have been allowed to invest in units of InvITs and REITs, such investment is contingent upon the Sponsor of the InvIT or the REIT having been assigned minimum 'AA' or equivalent rating from at least two credit rating agencies. This requirement seems a little misguided since the Sponsor would have limited operational involvement in the InvIT or the REIT, the important parameter would in fact be, the InvIT's/ REIT's rating.

Moreover, most Sponsors are likely to retain some assets, particularly under-construction assets, which may affect their credit rating. Additionally, since the consideration paid to the Sponsor for transfer of assets is likely to be units of the InvIT/ REIT in most instances, a general exemption for swap of Sponsors' shareholding in SPVs with units of InvITs/ REITs, even where the Sponsor is a foreign owned and controlled company would ease the listing process considerably. Lastly, the InvIT Regulations and REIT Regulations require that the transfer of assets to the InvIT/ REIT should be completed prior to the allotment of units in the public offer (and private placement, which is allowed only for InvITs). In case consideration to the Sponsor is paid in cash instead of units, this is bound to cause some difficulties as the InvIT/ REIT would be able to access issue proceeds only after listing and there are restrictions on commercial banks' ability to provide loans for acquisition of securities.

Whilst the Government of India and SEBI have played, and continue to play, a significant role in making InvITs and REITs a reality in India, it is important to note that regulatory regime pertaining to InvITs and REITs are fairly nascent and continue to evolve. In this regard, SEBI's guidance on post-listing obligations, such as applicability of SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011, SEBI (Prevention of Insider Trading) Regulations, 2015 (the "**PIT Regulations**") and SEBI (Listing Obligations and Disclousre Requirements) Regulations, 2015 (the "**LODR**") mechanism for other kinds of further offerings and mechanism for migration of InvITs listed on private placement basis to the framework for InvITs listed through a public offer process would provide much needed clarity and encourage many more developers to consider listing of InvITs and REITs. The Ministry of Finance, Government of India, has also played an important role in facilitating the establishment and growth of InvITs and REITs. The Central Board of Direct Taxes has provided a largely favourable tax regime and liberalised the ability of investors to invest in the units of InvITs and REITs. With the passage of time, InvITs and REITs, being innovative financial instruments, will provide the much needed impetus to infrastructure and real estate financing, thereby making it a success.

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COMPANY LAW UPDATE

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Substantive amendments to the Target Exemption under the Merger Control Regime notified

- The Ministry of Corporate Affairs ("**MCA**") has issued a notification ("**Notification**") amending the existing Target Exemption (*de minimis exemption*) notification. The Notification states that the Target Exemption, which was initially applicable only to acquisition transactions, now applies to both mergers and acquisitions. Accordingly, in case the target enterprise, whose shares/voting rights/assets/control is being acquired or which is being merged, has assets not exceeding INR 3.5 billion in India or turnover not exceeding INR 10 billion in India, the acquisition or merger will be exempt from the requirements of obtaining the Competition Commission of India's ("**CCI**") approval.
- Additionally, the notification has clarified that in case of an acquisition of assets or division of an enterprise, only the assets and turnover of the relevant target business or division being acquired will be considered for determining the notifiability. This is a transformation from the previous practice wherein the CCI required that the value of the entire assets and turnover of the seller enterprise (and not just that of the assets or division being acquired) be considered for determining notifiability of the transaction.
- For an analysis of the changes introduced by the Notification and implications, please refer to our blog post on the same.

(MCA Notification no. S.O. 988(E) published in Gazette on March 29, 2017)

Exemptions and modifications to provisions of the 2013 Act for specified companies in International Financial Services Centres

- In order to attract more companies to set-up shop in International Financial Services Centres ("**IFSC**") in India, the MCA has specified certain provisions of the 2013 Act that shall not apply, or apply with the certain exceptions, modifications and adaptations to unlisted public companies and private companies which are licensed to operate by the RBI or SEBI or the IRDAI from the IFSC located in an approved multi services Special Economic Zone ("**SEZ**") set-up under the SEZ Act, 2005 read with SEZ Rules, 2006.
- A specified IFSC company will be required to be to be incorporated only as a company limited by shares, and shall be required to have the suffix 'IFSC' or 'International Financial Service Company' as part of its name.
- IFSC companies, as specified above , have been exempted from, *inter alia*,:
  - the provisions relating to related party transactions in case of a holding, subsidiary or an associate of a specified IFSC company, or any other subsidiary of its holding company;
  - certain provisions relating to private placement of securities;
  - the restriction on issuance of sweat equity shares prior to the expiry of 1 year from the date of commencement of business;

- the requirement for a shareholders' special resolution for the issuance of further shares to employees of the company under an employees' stock option scheme;
- the restriction on purchasing or financing the acquisition of its own shares, subject to prescribed conditions;
- the requirement to convene the extraordinary general meetings of the company within India;
- the applicability of the secretarial standards relating to meetings of a company (SS-1) and board meetings (SS-2);
- the applicability of provisions relating to corporate social responsibility, for a period of 5 years from the commencement of business;
- the requirement to appoint a woman director and independent directors on their board of directors;
- the requirement for appointment of at least 1 director resident in India, for the first financial year post incorporation;
- the provisions relating to Audit Committee, Nomination and Remuneration Committee and Stakeholders' Relationship Committee;
- the restriction on having more than 2 layers of investment companies; and
- the requirement of obtaining shareholders' and Central Government approval and limitations on the remuneration payable to key managerial personnel.

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(*MCA Notifications G.S.R. 08(E) and 09(E) published in the Gazette on January 04, 2017*)

Amendments to the Companies (Incorporation) Rules, 2016

- The MCA has by way of the Companies (Incorporation) Amendment Rules, 2017 amended the Companies (Incorporation) Rules, 2016 with effect from January 30, 2017. Key changes are as below:
- Rule 18 has been substituted to provide that the Certificate of Incorporation shall be issued by the Registrar in Form No.INC-11 and it shall mention permanent account number ("**PAN**") of the company where it is issued by the Income Tax Department ("**IT Dept.**").
- Form SPICe (INC-32) has also been substituted so as to include the functionality of applying for company PAN and tax deduction and collection account number (TAN) (allotted by IT Dept.) in the SPICe form itself.

(*MCA Notification G.S.R. 70(E) published in the Gazette on January 27, 2017*)

Clarification on the applicability of winding up provisions of the 2013 Act to the closure of a place of business by foreign companies

- The MCA has clarified the scope of application of sub-section (2) of section 391 of the 2013 Act, which provides that Chapter XX of the 2013 Act i.e. the provisions relating to winding up, shall apply *mutatis mutandis* to the closure of a place of business in India by a foreign company as if it were a company incorporated in India.
- It has been clarified that sub-section (1) and (2) of Section 391 of the 2013 Act are to be read harmoniously and consequently provisions of sub-section (2) of Section 391 of the 2013 Act would apply only in case of a foreign company which has issued a prospectus or issued Indian Depository Receipts pursuant to the provisions of Chapter XXII of the 2013 Act.

(MCA General Circular 01/2017 dated February 22, 2017)

Amendments to the Companies (Transfer of Proceedings Rules) 2016

- The MCA has by way of the Companies (Transfer of Proceedings) Amendment Rules, 2017 amended the Companies (Transfer of Proceedings) Rules, 2016 (the "**Transfer Rules**") to extend, from 60 days to 6 months, the time period permissible to the petitioner for filing of the relevant information with the relevant bench of the NCLT, for the purposes of the transfer from the High Courts to the such bench of the NCLT, of pending proceedings for winding up of a company on grounds of 'inability to pay debts' in terms of Rule 5 of the Transfer Rules.

(MCA Notification No G.S.R. 175 (E) published in the Gazette on February 28, 2017)

Amendments to the Investor Education and Protection Fund Authority (Accounting, Audit, Transfer and Refund) Rules, 2016

- The MCA has by way of the Investor Education and Protection Fund Authority (Accounting, Audit, Transfer and Refund) Amendment Rules, 2017 ("**IEPF Amendment Rules**") amended the Investor Education and Protection Fund Authority (Accounting, Audit, Transfer and Refund) Rules, 2016 ("**IEPF Rules**").
- The IEPF Amendment Rules, *inter alia,* provide for:
    - the transfer of the shares due to be transferred to the Investor Education and Protection Fund("**IEPF**"), as well as any benefits accruing on such shares e.g., bonus shares, split, consolidation, fraction shares etc. (other than rights issue), directly to the demat account of the IEPF Authority (as opposed to a suspense account held with a depository which was the case earlier) and the procedure for such transfer;
    - mandatory dematerialisation of physical shares transferred to the demat account of the IEPF Authority; and
    - in respect of shares credited to the IEPF demat account as a result of dividend not having been paid or claimed for 7 consecutive years or more, re-transfer of such shares pursuant to a request of a claimant in the prescribed format and verification of such claim, only to the demat account of such claimant.

(MCA Notification No G.S.R. 178 (E) published in the Gazette on February 28, 2017)

Amendments to Schedule III of the 2013 Act and the Companies (Audit and Auditors) Rules, 2014 in view of demonetization

- The MCA has amended the Schedule III (*General Instructions for preparation of Balance Sheet and Statement of Profit and Loss of a Company*) of the 2013 Act to mandate the disclosure, in the balance sheet and the profit and loss statement of companies, of information relating to the demonetised currency notes of INR 500 and INR 1,000 held and transacted by the company during the period from November 08, 2016 to December 30, 2016.

- The MCA has also amended the Companies (Audit and Auditors) Rules, 2014 to include a new clause (d) to Rule 11 thereof which provides that the auditor's report shall include their comments on whether the company had provided requisite disclosures in its financial statements as to holdings as well as dealings in said notes during the period from November 08, 2016 to December 30, 2016 and if so, whether these are in accordance with the books of accounts maintained by the company.

(MCA Notifications No G.S.R. 307 (E) and 308 (E) published in the Gazette on March 30, 2017)

Amendments to the Companies (Meetings of Board and its Powers) Rules, 2014

- The MCA, has by way of the Companies (Meetings of Board and its Powers) Amendment Rules, 2017 (the "**Meetings Amendment Rules**"), slightly modified the thresholds for related party transactions, as specified in Rule 15(3)(a) of the Companies (Meetings of Board and its Powers) Rules, 2014, beyond which prior approval by way of an ordinary resolution at a shareholders' meeting of the company is required.

- Shareholders' approval would now be required for specified transactions 'amounting to 10 or more per. cent.' of the turnover or net worth of the company, as the case may be, as opposed to transactions 'exceeding 10 per. cent.' of the turnover or net worth.

(MCA Notification No G.S.R. 309 (E) published in the Gazette on March 30, 2017)

Amendments to the forms relating to registration and satisfaction of charges

- MCA has revised Forms CHG-1, CHG-4 and CHG-9 wherein certain declarations and field level changes have been incorporated to capture details *viz*. (i) ranking of charges, (ii) particulars of the principal terms and conditions of the charge, (iii) particulars of the property or asset(s) charged (including complete address and location of the property), (iv) description of document by which the borrower/third party acquired the title etc.

(This has not been published in the Gazette as on date)

Notification of the voluntary liquidation provisions of the Insolvency and Bankruptcy Code, 2016 and the rules thereunder

- The MCA has notified, *inter alia,* section 59 of the Insolvency and Bankruptcy Code, 2016 (the "**Code**") which relates to the voluntary winding up of corporate persons.
- With effect from April 01, 2017, all applications for voluntary winding up of a company would be required to be filed with the NCLT under Section 59 of the Code read with the Insolvency and Bankruptcy Board of India (Voluntary Liquidation process) Regulations, 2017 ("**Voluntary Liquidation Regulations**") which were notified by the Insolvency and Bankruptcy Board to take effect from April 01, 2017.
- The Voluntary Liquidation Regulations provides, *inter alia,* for initiation of the liquidation, appointment of the liquidator, powers and functions of the liquidator, the process to be followed (including proving and verification of claims, manner of realization of assets, distribution of assets, etc.).

(*MCA Notification No G.S.R. 1005 (E) published in the Gazette on March 30, 2017 and IBBI Notification No. IBBI/2016-17/GN/REG010 dated March 31, 2017*)

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FOREIGN INVESTMENT AND RBI UPDATES

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Prohibition on an Indian Party from making overseas direct investment in Non-Cooperative Countries/ Territories identified by Financial Action Task Force

- The Reserve Bank of India ("**RBI**") has, in order to align its instructions with the objectives of the Financial Action Task Force ("**FATF**"), decided to prohibit an Indian party from making direct investment in an overseas entity (*set up or acquired abroad, directly as a JV/ WOS, or indirectly as a step-down subsidiary*) located in countries identified by the FATF as 'non co-operative countries and territories' as per the list available on the FATF website (www.fatf-gafi.org) or as notified by the RBI from time to time.
- The RBI has also made a corresponding amendment to the relevant foreign exchange regulations *vide* the Foreign Exchange Management (Transfer or Issue of Any Foreign Security) (Second Amendment) Regulations, 2016, to give effect to such a prohibition.

(*FEM (Transfer or Issue of Any Foreign Security) (Second Amendment) Regulations, 2016 dated January 2, 2017 and A.P. (DIR Series) Circular No. 28 dated January 25, 2017*)

Issuance of convertible notes by Indian start-up companies

- The RBI has, *vide* the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident outside India) (Fifteenth Amendment) Regulations, 2016, permitted Indian start-up companies to issue convertible notes, where a 'convertible note' has been defined as "*an instrument issued by a start-up company evidencing receipt of money initially as debt, which is repayable at the option of the holder, or which is convertible into such number of equity shares of such start-up company, within a period not exceeding five years from the date of issue of the convertible note, upon occurrence of specified events as per the other terms and conditions agreed to and indicated in the instrument.*"

- The following conditions have been prescribed for the issuance of such convertible notes by the Indian start-up companies:

  - A person resident outside India (*other than an individual who is citizen of Pakistan or Bangladesh or an entity which is registered/ incorporated in Pakistan or Bangladesh*) may purchase convertible notes issued by an Indian start-up for an amount of atleast INR 2.5 million or more in a single tranche.

  - A start-up company engaged in an approval route sector will require Government approval prior to issuance of convertible notes to a non-resident.

  - The start-up shall receive the foreign investment by inward remittance through banking channels or by debit to the NRE/FCNR (B)/Escrow account maintained by the person concerned in accordance with the Foreign Exchange Management (Deposit) Regulations, 2016.

  - NRIs are permitted to acquire convertible notes on non-repatriation basis in accordance with the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident outside India) Regulations, 2000 ("**FEMA 20**").

  - A person resident outside India may acquire or transfer, by way of sale, convertible notes, from or to, a person resident in or outside India in accordance with RBI pricing guidelines after obtaining the prior approval of the Government in case of start-up companies engaged in an approval route sector.

  - The start-up company issuing convertible notes shall be required to furnish reports as prescribed by the RBI.

- The amendment is a specific exception to start-up companies and a departure from the existing foreign exchange policy, where optionally convertible debentures are considered External Commercial Borrowings.

(*FEM (Transfer or Issue of Security by a Person Resident outside India) (Fifteenth Amendment) Regulations, 2016 dated January 10, 2017*)

Amendments to FEMA 20 in relation to FDI in Securities Markets

- The RBI has, *vide* the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident outside India) (Amendment) Regulations, 2017, amended FEMA 20 to subsume commodity derivative exchanges within the category of 'Infrastructure company in the Securities Market' where foreign direct investment ("**FDI**") is permitted upto 49% under the automatic route. Any such foreign investment, including investments by foreign portfolio investors ("**FPIs**") will be subject to the guidelines/ regulations issued by the Central Government, the SEBI and the RBI.

(*FEM (Transfer or Issue of Security by a Person Resident outside India) (Amendment) Regulations, 2017 dated January 10, 2017*)

Delegation of power to regional offices of the RBI to compound contraventions under FEMA 20 without limit of amount of contravention

- The RBI has empowered its regional offices to compound the contraventions relating to delay in filing of the Annual Return on Foreign Liabilities and Assets ("**FLA Return**") by all Indian companies which have received FDI in the previous year(s) (including the current year).
- While there is no limit on the amount of contravention, the Kochi and Panaji regional offices are only permitted to compound contraventions for an amount below INR 10 million. The contraventions of INR 10 million or more will continue to be compounded at central office.

(RBI Circular A.P. (DIR Series) Circular No. 29 dated February 02, 2017)

Investment by Multilateral and Regional Financial Institutions in Rupee Denominated Bonds issued Overseas permitted

- The RBI has permitted Multilateral and Regional Financial Institutions where India is a member country to invest in Rupee denominated bonds issued overseas by Indian entities.

(RBI Circular A. P. (DIR Series) Circular No.31 dated February 16, 2017)

FDI in LLPs by investors other than FPI, FII or FVCI permitted

- The RBI has amended FEMA 20 to permit a person resident outside India (other than a citizen of Pakistan or Bangladesh) or an entity incorporated outside India (other than an entity in Pakistan or Bangladesh) not being FPIs, foreign institutional investors or foreign venture capital investors registered with the SEBI, to contribute foreign capital either by way of capital contribution or by way of acquisition/ transfer of profit shares in the capital structure of limited liability partnerships ("**LLPs**") by way of FDI.
- The scheme to be called the 'Foreign Direct Investment in Limited Liability Partnerships' (FDI-LLP) permits contribution to the capital of an LLP as an eligible investment, subject to the following conditions:
  - FDI is permitted under the automatic route in LLPs operating in automatic route sectors/ activities where 100% FDI is allowed through the automatic route and there are no FDI-linked performance conditions.
  - An Indian company or an LLP, having foreign investment, will be permitted to make downstream investment in another company/ LLP engaged in sectors in which 100% FDI is allowed under the automatic route where there are no FDI linked performance conditions. The onus shall be on the Indian company/ LLP accepting downstream investment to ensure compliance with the required conditions.
  - FDI in LLP will be subject to compliance with the conditions specified in the Limited Liability Partnership Act, 2008.

- A company having foreign investment can be converted into an LLP under the automatic route only if it is engaged in a sector where foreign investment up to 100% is permitted under the automatic route and there are no FDI linked performance conditions.

- FDI in an LLP (*either by way of capital contribution or by way of acquisition/ transfer of profit shares*) shall be at a price more than or equal to the fair price determined using any internationally accepted/ adopted valuation methodology as per market practice and accompanied by a valuation certificate issued by a chartered accountant or by a practicing cost accountant or a Central Government approved valuer.
- Payment towards capital contribution in LLPs shall be made by way of inward remittance through banking channels; or by debit to NRE/ FCNR(B) account of the person concerned.
- FDI in LLPs and disinvestment/ transfer of capital contribution or profit shares between a resident and a non-resident shall be reported to the RBI in the manner prescribed, and LLPs that have received FDI in the previous year(s) (*including the current year*) shall submit to the RBI, on or before the 15th day of July of each year, an FLA Return.

(FEM (Transfer or Issue of Security by a Person Resident outside India) (Second Amendment) Regulations, 2017, dated March 03, 2017)

FDI in the E-Commerce Sector permitted

- Pursuant to the Press Note 3 dated March 29, 2016 issued by the Department of Industrial Policy and Promotion, Ministry of Commerce and Industry, the RBI has amended Schedule I of FEMA 20 to allow 100% FDI in companies engaged in the marketplace model of e-commerce, subject to prescribed conditions. The term 'Market Place model of e-commerce' is defined as providing of an information technology platform by an e-commerce entity on a digital and electronic network to act as a facilitator between the buyer and the seller.
- FDI is not permitted in the 'Inventory based model of e-commerce', defined as an e-commerce activity where inventory of goods and services is owned by an e-commerce entity and is sold to the consumers directly.

(FEM (Transfer or Issue of Security by a Person Resident outside India) (Fourth Amendment) Regulations, 2017 dated March 09, 2017)

Amendments to the definition of "Infrastructure Lending" in the NBFC Master Directions

- The RBI has amended the definition of the term 'Infrastructure Lending' as set out in the Master Directions applicable to Non Banking Financial Companies ("**NBFCs**") to include a reference to 'Harmonised Master List of Infrastructure Sub Sectors' as updated by the Department of Economic Affairs, Ministry of Finance, Government of India, from time to time.
- The 'Harmonised Master List of Infrastructure Sub Sectors' was last updated on March 30, 2017 to include 'Affordable Housing' as a sub-sector under the 'Social and Commercial Infrastructure' category.

(RBI Circular No. DNBR.PD.CC.No.085/03.10.001/2016-17 dated March 02, 2017)

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SECURITIES LAW UPDATE

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Amendments and Notifications

Amendments to SEBI (Alternative Investment Funds) Regulations, 2012

With a view to encourage investments by angel funds, SEBI has amended the SEBI (Alternative Investment Funds) Regulations, 2012 ("**AIF Regulations**") to provide for the following:

- The upper limit for number of angel investors in a scheme has been enhanced from 49 to 200.
- Whilst angel funds were earlier permitted to invest in venture capital undertakings which were incorporated during the preceding 3 years from the date of such investment, this has been amended to provide that an angel fund can invest in start-ups, as defined by the Department of Industrial Policy and Promotion vide notification G.S.R 180(E) dated February 17, 2016.
- The minimum investment threshold for angel funds has been reduced from INR 5 million to INR 2.5 million.
- The lock-in period of an angel fund has been reduced from 3 years to 1 year.
- Additionally, an angel fund may also invest in the securities of companies incorporated outside India, subject to such conditions or guidelines as may be stipulated or issued by the RBI and SEBI from time to time.

(SEBI Notification No. SEBI/LAD-NRO/GN/2016-17/026, dated January 3, 2017, with effect from January 4, 2017)

Amendments to the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015

SEBI has amended the LODR to provide for the following:

- Regulation 26 has been amended to provide that employees including key managerial personnel or directors or promoters of a listed company shall not enter into any agreement for themselves or on behalf of any other person, with any shareholder or any other third party with regard to compensation or profit sharing in connection with dealings in the securities of such listed entity, unless prior approval for the same has been obtained from the board of directors of the company as well as public shareholders by way of an ordinary resolution.
- The aforementioned agreements, if any, whether subsisting or expired, entered during the preceding 3 years from the date of the amendment, shall be disclosed to the stock exchanges for public dissemination. Further, such subsisting agreements shall be placed for approval before the board in the forthcoming board meeting and if approved by the board, shall be placed before the public shareholders for approval by way of an ordinary resolution in the forthcoming general meeting. All 'interested persons' (defined therein) involved in the transaction covered under the agreement shall abstain from voting in the general meeting.
- SEBI has also made certain amendments to Regulation 37 (*Draft Scheme of Arrangement and Scheme of Arrangement*), the details of which are covered in the lead article in this issue of *Insight*.

(SEBI Notification No. SEBI/LAD-NRO/GN/2016-17/025, dated January 3, 2017, with effect from January 4, 2017; SEBI Notification No. SEBI/LAD/NRO/GN/2016-17/029 dated February 10, 2017, with effect from February 15, 2017)

Modification of the guidelines for participation of Eligible Foreign Investors and FPIs in IFSCs

In order to encourage participation by Eligible Foreign Investors ("**EFIs**") and FPIs in the Government's new IFSC initiative, SEBI has issued a circular in partial modification of the SEBI (IFSC) Guidelines, 2015, pursuant to consultations held with the stakeholders on the regulatory framework on participation of EFIs. The circular, *inter alia*, provides for the following:

- FPIs are permitted to set up operations in IFSCs without any additional documentation or prior approval.
- In case of participation of FPIs in IFSC, a trading member of the recognized stock exchange in IFSC may rely upon the due diligence process already carried out by a SEBI registered intermediary during the course of registration and account opening process in India. In case of participation of an EFI, which is not registered with SEBI as an FPI, but desirous of operating in IFSC, a trading member of the recognized stock exchange in IFSC may rely upon the due diligence carried out by a bank, permitted by the RBI to operate in IFSC, during the account opening process of EFI.
- FPIs which presently operate in Indian securities market and propose to operate in IFSC are required to ensure clear segregation of funds and securities. Custodians are required to monitor compliance of the same for their respective FPI clients. Such FPIs are required to keep their respective custodians informed about their participation in IFSC.
- Recognised stock exchanges in IFSC are, at all times, required to maintain necessary details of EFIs, which may be called upon by SEBI/ RBI or any other authority.

(SEBI Circular No. IMD/ HO/ FPIC/ CIR/ P/ 2017/ 003 dated January 4, 2017)

SEBI guidance note on Board Evaluation

In view of the provisions of the 2013 Act and the LODR, which mandate evaluation of the board of a listed company, SEBI has issued a detailed guidance note for evaluation of boards of listed companies including the role of independent directors, to help them improve the evaluation process, derive the best possible benefit and achieve the objective of the entire process as well as to improve their corporate governance. This may be adopted by listed companies as considered appropriate. The guidance note covers all major aspects of board evaluation and provides, *inter alia,* that:

- The role and function of chairperson in board evaluation should be laid out clearly in advance in order to achieve maximum benefit of the process.
- The nomination and remuneration committee should:
  - formulate the criteria for evaluation of performance of independent directors and the board of directors;
  - carry out evaluation of every director's performance;
  - determine whether to extend or continue the term of appointment of the independent director, on the basis of the report of performance evaluation of independent directors.
- The independent directors of the listed entity should hold a meeting at least once a year separately. In such a meeting, independent directors should review the performance of non-independent directors and the board as a whole including the chairperson.

➢ The performance evaluation of independent directors should be done by the entire board, excluding the director being evaluated.
➢ A statement indicating the manner in which formal annual evaluation has been made by the board of its own performance and that of its committees and individual directors should be included in the report by the board of directors placed in the general meeting. Further, the performance evaluation criteria for independent directors should be disclosed in the annual report of the company.
➢ Criteria for every evaluation may be decided at every level depending on the functions, responsibilities, competencies, etc. Several indicative criteria for evaluation have been specified in the guidance note.
➢ The guidance note further refers to the mandatory disclosures required under the 2013 Act and the LODR regarding board evaluation by listed entities.
➢ This board evaluation report will prove an invaluable tool in due diligence of listed companies.

(SEBI Circular No. SEBI/HO/CFD/CMD/CIR/P/2017/004, dated January 5, 2017)

Extension of time period for submission of action plan by exclusively listed companies of de-recognized/non-operational/exited stock exchanges placed in the dissemination board

➢ SEBI had on January 05, 2017 extended up to March 31, 2017 the time period permissible to exclusively listed companies of de-recognised / non-operational / exited stock exchanges which are placed in the dissemination board, for submission to the designated stock exchanges, of the plan of action for listing / providing exit to their shareholders. Pursuant to its circular dated March 27, 2017, SEBI has further extended the time to June 30, 2017.

(SEBI Circular No. SEBI/HO/MRD/DSA/CIR/P/2017/5 dated January 05, 2017 and SEBI Circular No. SEBI/HO/MRD/DSA/CIR/P/2017/27 dated March 27, 2017)

Amendments to SEBI (Foreign Portfolio Investors) Regulations, 2014

SEBI has amended the SEBI (Foreign Portfolio Investors) Regulations, 2014 (“**FPI Regulations**”) to provide for the following:
➢ FPIs have been permitted to invest in the following instruments: • unlisted debt securities or securitised debt instruments; • unlisted non-convertible debentures/bonds issued by an Indian company, subject to the guidelines issued by the MCA, Government of India from time to time; and • securitized debt instruments, including (a) any certificate or instrument issued by a SPV set up for securitization of assets with banks, financial institutions or nonbanking financial institutions as originators; and (b) any certificate or instrument issued and listed in terms of the SEBI (Public Offer and Listing of Securitised Debt Instruments) Regulations, 2008.

- The requirement of transacting in securities only through stock brokers will not apply to:
  - transactions by Category I and II FPIs in corporate bonds; and
  - transactions on the electronic book provider platform of recognized stock exchanges.

(SEBI Notification dated January 11, 2017, and SEBI Notification dated February 27, 2017)

Procedures for Exchange Listing Control Mechanism

SEBI has issued a circular on January 27, 2017, prescribing certain conditions in case of a stock-exchange listing on another stock-exchange under Regulation 45 of the SEBI (Stock Exchanges and Clearing Corporations) Regulations, 2012. In order to ensure effective compliance with the applicable laws in such a situation, the circular provides for the following:

- The listing department of the listing stock exchange i.e. where the other stock exchange is getting listed will monitor the compliance of the stock-exchange getting listed;
- The independent oversight committee of the listing stock exchange will exercise oversight at the second level to deal with conflicts, if any. The stock-exchange getting listed may appeal to such committee if aggrieved from the decision of the listing department of the listing stock exchange; and
- The independent conflict resolution committee appointed by SEBI will monitor potential conflicts between the listing stock exchange and the stock exchange getting listed, on a regular basis. If the stock exchange getting listed is aggrieved by the decision of the independent oversight committee of the listing stock exchange, then it may appeal to this committee.

(SEBI Circular No. SEBI/HO/MRD/DSA/CIR/P/2017/9 dated January 27, 2017)

Integrated Reporting by Listed Entities

- SEBI has made it mandatory for the top 500 listed entities under Regulation 34(2)(f) of the LODR to submit Business Responsibility Report (**"BRR"**). Key principles which are required to be reported by the entities pertain to areas such as environment, governance, stakeholder's relationships, etc. The integrated report needs to be prepared on the guiding principles prescribed by the International Integrated Reporting Council.
- Accordingly, SEBI has advised the listed entities to adhere to the following:
  - Integrated Reporting may be adopted on a voluntary basis from the financial year 2017-18 by top 500 companies which are required to prepare BRR;
  - The information related to Integrated Reporting may be provided in the annual report separately or by incorporating it in the Management Discussion and Analysis or by preparing a separate report (annual report prepared as per integrated reporting framework);

- In case the company has already provided the relevant information in any other report prepared in accordance with national/international requirement / framework, it may provide appropriate reference to the same in its Integrated Report so as to avoid duplication of information; and

- The companies may host the Integrated Report on their website and provide appropriate reference to the same in their Annual Report.

(SEBI Circular No. SEBI/HO/CFD/CMD/CIR/P/2017/10 dated February 6, 2017)

Minutes of the SEBI Board Meeting held on February 11, 2017

SEBI, in its board meeting held in New Delhi on February 11, 2017, made *inter alia* the following decisions:

➢ Major *initiatives proposed for the financial year 2017-18:*

- Reducing the listing time gap by bringing down the issue timing from the existing requirement of T+6;

- Allowing institutional participation in commodity derivatives markets in a phased manner;

- Facilitating integration between commodity spot markets and derivatives markets;

- Designing a system of risk based supervision for commodity brokers;

- Setting up a cyber security lab for the securities market;

- Allowing listing and trading of securitization receipts issued by assets reconstruction companies;

- Facilitating the objective of 'ease of doing business', introduction of common application form for registration, opening of bank and demat accounts, and issue of PAN for foreign portfolio investors;

- Setting up a facility for online registration of intermediaries;

- Strengthening the research initiatives in SEBI with special focus on research on commodity market, interlinkages of various markets such as equity, forex, and commodity etc.;

- Increasing its efforts in the areas of investor education / financial education, covering all the districts in the country; and

- Enhancing engagement in the social and digital media for investor awareness programmes.

➢ *Review of the working of Market Infrastructure Institutions (**"MIIs"**):* The Board approved the proposal of the Dr. Bimal Jalan Committee for a comprehensive review of the Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporations) Regulations, 2012 and SEBI (Depositories and Participants) Regulations, 1996.

(Minutes of the SEBI Board Meeting dated February 11, 2017)

Amendments to the SEBI (Issue and Listing of Debt Securities by Municipalities) Regulations, 2015

- SEBI has notified the SEBI (Issue and Listing of Debt Securities by Municipalities) (Amendment) Regulations, 2017, whereby SEBI amended the eligibility criteria of municipalities to issue debt securities to the public under Regulation 4.
- It provides that a municipality is required to have surplus income as per its income and expenditure statement, in any of the immediately preceding 3 financial years. This is in addition to the position prior to the amendment which required that a corporate municipal entity should not have a negative net worth in any of the immediately preceding 3 financial years.
- Further, the amendment introduced an additional eligibility criterion for a municipality issuing debt securities to the public, that is, it should not have defaulted in the repayment of debt securities or loans obtained from banks/financial institutions in the past 365 days.

(SEBI Notification No. SEBI/LAD/NRO/GN/2016-17/032 dated February 15, 2017)

Amendments to the ICDR

- SEBI has notified the SEBI (Issue of Capital and Disclosure Requirements) (Amendment) Regulations, 2017, whereby SEBI introduced specific liabilities for the contravention of the ICDR by a listed entity *vide* Regulation 111A including, *inter alia,* imposition of fines/suspension of trading and freezing of promoter/promoter group holding.
- It also introduced Regulation 111B which lays down the liability of a listed entity in case it fails to pay the fine imposed by any recognized stock exchange within the specified time.

(SEBI Notification No. SEBI/LAD/NRO/GN/2016-17/030 dated February 15, 2017)

Amendments to the SEBI (Mutual Funds) Regulations, 1996 regarding investment in InvITs and REITs

- SEBI has notified the SEBI (Mutual Funds) (Amendment) Regulations, 2017, whereby SEBI amended Regulation 2 and the seventh schedule of the SEBI (Mutual Funds) Regulations, 1996 ("**MF Regulations**").
- It provides for:
  - Inclusion of the definition of an InvIT and a REIT;
  - Conditions for a mutual fund to invest in the units of an InvIT or REIT i.e. (a) a mutual fund under all its schemes cannot own more than 10% of units issued by a single issuer of REIT and InvIT; and (b) a mutual fund scheme cannot invest more than 10% of its net asset value in the units of REIT and InvIT and more than 5% of its net asset value in the units of REIT and InvIT issued by a single issuer. This limitation is not applicable to investments in case of an index fund or a sector/industry specific scheme pertaining to InvIT or REIT.

- Pursuant to this amendment, SEBI on February 28, 2017 issued a circular stating that the above mentioned conditions shall be applicable to all fresh investments by all schemes, including an existing scheme. Any existing scheme intending to invest in units of REITs/InvITs shall be required to abide by the provisions of Regulation 18 (15A) of the MF Regulations. For investment in units of REITs/InvITs by an existing mutual fund scheme, unitholders of the scheme should be given a time period of at least 15 days for the purpose of exercising the exit option.

(SEBI Notification No. SEBI/LAD/NRO/GN/2016-17/031 dated February 15, 2017 and SEBI circular SEBI/HO/IMD/DF2/CIR/P/2017/17 dated February 28, 2017)

Amendments to the SEBI (Settlement of Administrative and Civil Proceedings) Regulations, 2014

- SEBI has notified the SEBI (Settlement of Administrative and Civil Proceedings) (Amendment) Regulations, 2017 on February 27, 2017.
- The amendment, *inter alia,* provides for:
  - filing of application for condonation of delay along with additional fees and enhancement in the settlement amount (where the application is filed after 60 calendar days from the expiry of the period specified);
  - refilling of rejected and withdrawn applications subject to facts and circumstances of each case and upon payment of additional fees and/or interest as recommended by the high powered advisory committee; and
  - stricter timeline for remitting payment of settlement amount, among others.

(SEBI Notification No. SEBI/LAD/NRO/GN/2016-17/036 dated February 27, 2017)

Investments by FPIs in corporate and Government debt securities

Pursuant to the amendments made in the FPI Regulations (as specified above), as well as the RBI's circulars A.P. (DIR Series) Circular No. 19 and A.P.(DIR Series) Circular No. 43 dated November 17, 2016 and March 31, 2017, respectively, in relation to investments by FPIs in corporate and Government debt securities, SEBI has provided for the following:

- FPIs may invest in unlisted non-convertible debentures/bonds issued by an Indian company subject to minimum residual maturity of 3 years and end use-restriction on investment in real estate business (as defined in FEMA 20), capital markets and purchase of land.
- The custodians of the FPIs are required to put in place an appropriate mechanism to ensure compliance with the conditions as prescribed by the RBI from time to time.
- Investment by FPIs in the unlisted corporate debt securities and securitised debt instruments shall not exceed INR 350 billion within the extant corporate debt limit which currently is INR 2443.23 billion.
- Investment by FPIs in securitised debt instruments shall not be subject to the minimum 3 year residual maturity requirement.

- Limit for FPIs in Central Government securities has been enhanced from INR 1520 billion to INR 1849.01 billion.
- Limit for long term FPIs (Sovereign Wealth Funds (SWFs), Multilateral Agencies, Endowment Funds, Insurance Funds, Pension Funds and Foreign Central Banks) in Central Government securities has been enhanced from INR 680 billion to INR 460.99 billion.
- Limit for investment by all FPIs in State Development Loans has been enhanced from INR 210 billion to INR 270 billion.
- All other existing terms and conditions in relation to investment in corporate debt securities and Government securities shall continue to apply to the FPIs.

(SEBI Circular No. SEBI/HO/IMD/FPIC/CIR/P/2017/16, dated February 28, 2017, and SEBI Circular No. IMD/FPIC/CIR/P/2017/30, April 3, 2017)

Amendments to the SCRR

- The Department of Economic Affairs, Ministry of Finance, Government of India has on March 20, 2017 notified the Securities Contracts (Regulation) Amendment Rules, 2017. The amendment *inter alia* provides that a category I and category II FPI registered as such may be admitted as a member of the recognized stock exchange if recommended by SEBI, by relaxing the qualifications required for obtaining the membership of such a stock-exchange. An FPI so recognized as a member shall only undertake proprietary trades in such class of securities, as are specifically permitted by SEBI.

(Notification No. G.S.R. 268(E) published in the Gazette on March 20, 2017)

Informal Guidance

Informal Guidance on the SEBI (Portfolio Managers) Regulations, 1993

- SEBI has, on an application made by Karvy Stock Broking Limited ("**Karvy**"), clarified to Karvy, that in relation to the SEBI (Portfolio Managers) Regulations, 1993, specifically Regulation 16, a portfolio manager can keep the funds of all the clients in a separate bank account maintained by it, and may capture the same in the demat account of its resident Indian clients.

(SEBI Informal Guidance No. IMD/ DoF-1/30106/ 2016 dated November 02, 2016 published on February 01, 2017)

Informal Guidance regarding 'connected person' under the PIT Regulations

- Prabhudas Lilladher Private Limited ("**PLPL**") made an application to SEBI under the Informal Guidance Scheme for seeking clarification, *inter alia*, regarding:

  - the applicability of the code of conduct formulated by a company in terms of the PIT Regulations to persons with seniority and professional designation who do not have access to unpublished price sensitive information; and

  - whether a written declaration to rebut the presumption of being a connected person by a financially independent spouse of an employee/designated person is sufficient to exclude such spouse from the purview of code of conduct for employee trading.

- In this regard, SEBI clarified to PLPL that:

  - The employees and connected persons are designated on the basis of functional role and not only on the basis of seniority.

  - The code of conduct applies to all connected persons and not only to designated persons. The designated persons are specified by the board of directors in consultation with the compliance officer.

  - The guidance note on PIT Regulations dated August 24, 2015 states that a spouse is presumed to be an 'immediate relative', unless rebutted. The sufficiency and validity of a written declaration from a spouse for the purposes of excluding such person from the code of conduct of a company can only be ascertained on a case to case basis by the company.

(SEBI Informal Guidance No. ISD/OW/34644, dated December 23, 2016 published on April 06, 2017)

Informal Guidance issued in relation to responsibilities of registrars to the issue in connection with an initial public offer

- SEBI has, on an application made by SBI Capital Markets Limited (**"SBI"**), clarified to SBI, that in relation to the activities required to be carried out by the respective intermediaries in connection with an initial public offer, registrars to the issue are responsible to discharge their duties as per their roles and responsibilities laid down by SEBI, including *inter alia*, the ICDR, the SEBI Circular CIR/CFD/POLICYCELL/11/2015 dated November 10, 2015 and the 12 circulars referred therein and the General Information Document.
- Further, it clarified that registrars to the issue are also required to fulfil their obligations as per the SEBI (Registrars to the Issue and Share Transfer Agents) Regulations, 1993 in a prompt, ethical and professional manner, exercise due diligence, ensure proper care and exercise independent professional judgment while making all reasonable efforts to avoid misrepresentation.

(SEBI Informal Guidance No. CFD/DIL-III/NR/AEA/OW/2016/35335 dated January 02, 2017 published on January 02, 2017)

Informal Guidance regarding pre-clearance request for acquisition of shares under PIT Regulations

- Kirloskar Chillers Private Limited ("**KCPL**"), forming part of the promoter group of Kirloskar Brothers Limited ("**KBL**"), for the purposes of acquiring shares in KBL, made an application to the compliance officer of KBL for pre-clearance in terms of the code of conduct ("**PIT Code**") formulated by KBL as mandated under the PIT Regulations . The application was rejected by the compliance officer on extraneous grounds.

  Therefore, KCPL approached SEBI, *inter alia*, for seeking clarification on the requirement of taking pre-clearance and whether the compliance officer can reject pre-clearance on grounds which are extraneous to the powers conferred to him in terms of the PIT Regulations and the PIT Code.

- In this regard, SEBI clarified to KCPL that:

  - The pre-clearance requirement, as mandated under the PIT Regulations, is required to be obtained only by 'designated persons' if the value of the proposed trade is above such thresholds as stipulated by the board of directors of the concerned company.

  - Thus a promoter, if designated as a 'designated person' by the board of directors in consultation with the compliance officer (based on their role in the management of the listed entity and access to unpublished price sensitive information), will be required to obtain pre-clearance for trading.

  - The compliance officer acts under the overall supervision of the board of directors or the audit committee, and as such, any question with respect to the act of compliance officer whether or not extraneous to the powers so conferred according to the PIT Regulations and the PIT Code, may be referred to the board of directors and the audit committee for examination in accordance with the extant laws and the relevant facts of the case.

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(SEBI Informal Guidance No. ISD/ OW/ 2700/ 2017, dated February 03, 2017 published on March 16, 2017)

Informal Guidance on pre-preferential allotment shareholding of allottees

- Balasore Alloys Limited ("**BAL**"), in relation to a preferential allotment made to a promoter group company ("**Preferential Allotment**") in accordance with the provisions of the ICDR, approached SEBI for seeking clarification on whether the promoters/ promoter group, who are not the allottees of the Preferential Allotment, are subject to any restriction to transfer/ sell their free equity shares, and whether the lock-in provisions, as specified in sub-regulation (6) of Regulation 78 of the ICDR are applicable to such promoters/ promoter group.
- In this regard, SEBI has clarified to BAL that:

  - The expression 'pre preferential shareholding of allottees' used in sub-regulation (6) of Regulation 78 (*Lock-in of specified securities*) of the ICDR refers only to the shareholding of the allottees and not to the promoters/ promoter group.

  - Therefore, the promoters/ promoter group who are not the allottees in the Preferential Allotment would not be under any restriction to sell their holding of free equity shares.

(SEBI Informal Guidance No. CFD/ DIL-1/ NS/ 2017/ 02660/ 1, dated February 07, 2017 published on March 06, 2017)

Consultation Papers

Consultation paper on enhancing disclosures in case of public issuance of non-convertible debentures having credit rating below investment grade

- SEBI has in relation to the public issuances of non-convertible debentures, proposed the introduction of *inter alia* the following:

- A pictorial representation of credit rating in the form of a 'Risk-o-Meter' or 'Rate-o-Meter';
- Enhancing disclosures in relation to credit rating in advertisements; and
- Restriction on the investment amount for retail investors for below investment grade issuances in order to add a layer of protection for them.

(SEBI Consultation paper dated January 04, 2017)

Addendum to the consultation paper on public issuance of non-convertible redeemable preference shares and debt securities by Municipalities

- SEBI has in relation to non-convertible redeemable preference shares ("**NCRPS**") and debt securities issued by municipalities, put forth proposals similar to the ones laid down in the SEBI Consultation Paper dated January 04, 2017 in relation to 'Enhancing Disclosures and Introduction of Risk-o-meter in case of public issuance of Non-convertible Debentures having credit rating below Investment Grade'.
- One of the additional proposals put forth by SEBI was the removal of the minimum credit rating requirement for the public issuance of NCRPS and debt securities by municipalities to bring it in line with the SEBI (Issue and Listing of Debt Securities) Regulations, 2009.

(SEBI Consultation paper dated January 16, 2017)

Consultation paper on consolidation and reissuance of debt securities

- SEBI has proposed a mechanism for consolidation and re-issuance of debt securities with a view to reducing fragmentation and enhancing liquidity in the secondary corporate bond market. The consultation paper proposes the following:
- Passive consolidation by way of:
  - restriction on the maximum number of International Securities Identification Numbers ("**ISINs**") in a year to only one per quarter or every two months to encourage issuers to consolidate issuances of debt securities under the same ISIN. One of the reasons for the lack of trading volume is non-availability of sufficient floating stock for each ISIN; and
  - staggered repayments of the redemption amount in order to avoid the situation of liquidity mismatch and bunching of liabilities for the issuer in case the above mentioned restriction is implemented; and
- Active consolidation by way of switching /conversions through methods explained therein. A bond switching or conversion is a repurchase in advance of maturity, where other debt securities would be supplied as payment.

(SEBI Consultation paper dated February 02, 2017)

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The views expressed in this newsletter do not necessarily constitute the final opinion of Cyril Amarchand Mangaldas on the issues reported herein and should you have any queries in relation to any of the issues reported herein or on other areas of law, please feel free to contact us at the following co-ordinates:

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