

ACUITY LAW

**SECURITIES
LAW NEWSLETTER**

JULY 2019
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ABOUT ACUITY LAW

Acuity Law was founded in November 2011. Acuity Law comprises of a team of young and energetic lawyers led by Souvik Ganguly and Gautam Narayan, who have deep and diverse experiences in their chosen areas of practice. We advise Indian and multinational companies, funds, banks and financial institutions, founders of companies, management teams, international law firms, domestic and international investment banks, financial advisors and government agencies in various transactions in and outside India.

Acuity Law takes pride in rendering incisive legal advice taking into consideration commercial realities. Our areas of practice are divided into two departments.

The Corporate practice is led by Souvik Ganguly and the Disputes practice is led by Gautam Narayan.

As part of the Corporate practice, Acuity Law advises on:

- Mergers and acquisitions;
- Distressed mergers and acquisitions;
- Insolvency Law;
- Private Equity and Venture Funding;
- Employment and labour laws;
- Commercial and trading arrangements; and
- Corporate Advisory

As part of the Disputes practice, Acuity Law under the leadership of Gautam Narayan advises and represents clients on domestic and cross - border:

- Civil disputes;
- Criminal law matters; and
- Arbitration matters

Acuity Law actively follows legislative and policy developments in its chosen areas of practice and shares such developments with clients and friends on a regular basis.

If you want to know more about Acuity Law, please visit our website acuitylaw.co.in or write to us at al@acuitylaw.co.in.

INTRODUCTION

This newsletter covers key updates about the developments in Indian securities law during the month of July 2019. We have summarized the key regulatory developments including (a) an order passed by the Securities Appellate Tribunal observing that non-executive directors of a company can be held liable for the non-compliance of the company; (b) circular issued by Securities and Exchange Board of India (**SEBI**) on disclosure of divergence in the asset classification and provisioning by banks; (c) amendments made to SEBI regulations to incorporate superior voting rights shares provision and; (d) a consultative paper by SEBI on resignation of statutory auditors from listed entities.

Please see below the summary of the relevant regulatory developments.

NON-EXECUTIVE DIRECTOR LIABLE FOR NON-COMPLAINE

Matter: Sheikh Abdul Rabial vs. Securities and Exchange Board of India

Order Dated: 2 July 2019

Summary:

SEBI's whole time member had passed an order (**impugned order**) against Sheikh Abdul Rabial (**Appellant**), director of Angel Rural Development Limited, for issuing secured redeemable non-convertible debentures by appointing an unregistered debenture trustee. The Appellant was held to be in violation of the Companies Act, 1956 and SEBI Act, 1992.

Appellant contended that he was a non-executive director and was not involved in the administration of the company or in the day to day affairs of the company.

However, the Securities Appellate Tribunal upheld the impugned order and observed that any type of director of a company can be held liable for the acts of the company if he is involved in the act in question. It is irrelevant whether that director is involved in the day to day affairs of the company.

MODIFICATION OF THE CIRCULAR ON DISCLOSURE OF DIVERGENCE IN THE ASSET CLASSIFICATION AND PROVISIONING BY BANKS

SEBI had issued a circular dated 18 July 2017, on the disclosure requirements for divergence in asset classification and provisioning by banks with listed securities. The circular stated that banks should disclose to the stock exchanges, divergences in the asset classification and provisioning when the additional provisioning requirements assessed by Reserve Bank of India exceed 15% of the published net profits after tax for the period preceding the filing of the annual financial statement by the banks.

The threshold of the additional provisioning has been modified to 10% of the reported profit before provisions and contingencies for the reference period.

SUPERIOR VOTING RIGHTS SHARES: AMENDMENT TO SEBI REGULATIONS

Post the release of the consultation paper by SEBI on 20 March 2019 and a framework on 27 June 2019, for issue of differential voting right shares, SEBI has amended regulations to insert provisions relating to superior voting rights (**SR**) shares.

I. SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015:

Issue: The listed entity having outstanding SR equity shares may issue SR equity shares to its promoter/founders only through a bonus, split or rights issue in accordance with the provisions of the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018 and the Companies Act, 2013.

Validity: The SR shares are required to be converted into equity shares having ordinary voting rights, five years post the date of initial listing of ordinary shares or at any time before the completion of five years. The validity of the SR shares can be extended for another five years by passing a resolution in which the SR shareholders will not be permitted to vote.

Voting rights:

- i. The SR shares shall be treated at par with the ordinary equity shares in every respect, except in the case of voting on resolutions. The SR equity shares shall be treated as ordinary equity shares in the circumstances listed, including appointment/removal of independent director/auditor, related party transactions involving SR shareholder, voluntary winding up of the listed entity.
- ii. Demise, resignation of the promoter holding the SR shares, merger or acquisition of a listed entity having the SR shares, where control would no longer remain with the SR shareholders or sale of the SR shares post the lock-in period but prior to lapse of validity of the SR shares by the SR shareholder, shall lead to compulsory conversion of SR equity shares into ordinary equity shares.

Independent directors: In the listed entity having SR equity shares the audit committee shall only comprise of independent directors, at least half of the board of directors shall comprise of independent directors, two-thirds of the nomination and remuneration committee, stakeholders relationship committee and risk management committee shall have independent directors.

II. SEBI (Issue of capital and disclosure requirements) Regulations, 2018 (ICDR):

To incorporate the introduction of SR shares, corresponding amendments were made to ICDR. The provision on eligibility requirements for an initial public offer now states that an SR equity shareholder shall make a public offer of only ordinary shares subject to the compliance of the conditions given therein including that the SR shares (a) had been held for a period of 6 months prior to filing of red herring prospectus; (b) have same face value as that of ordinary shares and be equal in all respects except voting rights; (c) were issued only to executives; and (d) have minimum voting rights of 2:1 up to a maximum of 10:1 compared to ordinary shares.

The provisions regarding the requirements during the initial and further public offer, on minimum promoter contribution, lock-in of specified shares held by promoters, pledge, transfer and general conditions to rights issue, restrictions on bonus issue have been amended to include SR shares accordingly.

III. SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 (Takeover code):

The increase in voting rights beyond the threshold limit without the acquisition of control, pursuant to the conversion of SR equity shares into ordinary shares has been exempted from the open offer obligation.

IV. In SEBI (Delisting of equity shares) Regulations, 2009 and SEBI (Buy-Back of Securities) Regulations, 2018, the definition of 'shares' now include SR equity shares.

CONSULTATIVE PAPER IN POLICY PROPOSALS WITH RESPECT TO RESIGNATION OF THE STATUTORY AUDITORS FROM LISTED ENTITIES

There have been a number of abrupt resignations by statutory auditors without completing their responsibilities citing 'pre-occupation' as the reason for resignation. Taking note of such resignations, SEBI has issued policy proposals on the subject to strengthen disclosures to investors and clarify the role of the audit committee.

Proposals:**Conditions for resignation of auditors**

- i. If the auditor of a listed entity proposes to resign – (a) after signing the audit report for all quarters (limited review/ audit) of a financial year except the last quarter, then the auditor would be required to finalize the audit report for the said financial year before such resignation; and (b) in all other cases, the auditor would be required to issue limited review / audit report for that quarter before such resignation.
- ii. If the auditor of a material unlisted subsidiary of the listed entity proposes to resign, then the auditor would be required to issue the limited review/audit report for that financial year / quarter, as applicable, before such resignation.
- iii. If the reason for the auditor's resignation is that the listed entity or a material unlisted subsidiary of a listed company is not providing information, the auditor would be required to provide an appropriate disclaimer in its audit report, in accordance with standard of auditing suggested by the Institute of Chartered Accountants of India.

Disclosures and role of audit committee

The auditors shall inform the audit committee any concerns regarding non-receipt of information or non-cooperation by the management and the committee shall communicate its views to the management and the auditor. The listed entity shall also disclose the audit committee's views to the stock exchanges.

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