ACUITY LAW

SECURITIES
LAW NEWSLETTER

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ACUITY LAW

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 June 2019. We have summarized the key regulatory developments including a press release by Securities and Exchange Board of India (**SEBI**) on (a) framework for issuance of differential voting rights shares by tech companies; (b) disclosure of encumbrances; informal guidance issued by SEBI on (c) applicability of SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018, on companies listed only on regional stock exchange(s); (d) requirement of a company with only debt securities listed to file financial results on consolidated basis under Regulation 52 of the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2018; and a circular issued by SEBI on (e) introduction of futures on commodity indices in commodity derivative segment.

We have also covered a discussion paper issued by SEBI on informant reward policy for insider trading cases.

Please see below the summary of the abovementioned regulatory developments.

FRAMEWORK FOR ISSUANCE OF DIFFERENTIAL VOTING RIGHTS

SEBI at its board meeting on 27 June 2019 approved the framework for issuance of differential voting rights shares by tech companies (i.e. intensive in the use of technology, information technology, intellectual property, data analytics, bio-technology or nano-technology to provide products, services or business platforms with substantial value addition).

The key elements of the framework have been enumerated below:

Eligible company:
Tech companies which have issued superior voting rights shares (**SR shares**) are permitted to do an initial public offering (**IPO**) of only ordinary shares.

The tech companies are required to fulfill the requirements of the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018 (**ICDR Regulations**) and the following conditions:

i) SR shareholders must be promoter/founder who hold executive position in the company.
ii) SR shareholders collective net worth should not exceed INR 500 crores.
iii) SR shares have to be held for at least for 6 months before filing of red herring prospectus.
iv) SR shares should have the voting rights of at least 2:1 and not more than 10:1 compared to ordinary shares.

Lock-in:
SR shares have to be listed post the IPO but will be locked-in until their conversion to ordinary shares. SR shares cannot be transferred between the promoters and there can be no pledge/lien over these shares.

Rights of SR shares:
The total voting rights of SR shareholders (including ordinary shares) post listing has been capped at 74%.

Enhanced corporate governance:
At least half of the Board and 2/3rd of the committees as prescribed under the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2018 (**LODR Regulations**) have to comprise of independent directors. The audit committee has to only comprise of independent directors.

Coat-tail Provisions:
Post IPO, the SR shares will be treated as ordinary shares (i.e. one SR share will have only one vote) in terms of voting rights in following circumstances:

i) Appointment or removal of independent directors and/or auditor;
ii) In case where promoter is willingly transferring control to another entity;
iii) Related party transactions in terms of LODR Regulations involving SR Shareholder;
iv) Voluntary winding up of the company;
v) Changes in the company's Article of Association or Memorandum- except any changes affecting the SR instrument;
vi) Initiation of a voluntary resolution plan under Insolvency and Bankruptcy Code, 2016;
vii) Utilization of funds for purposes other than business;
viii) Substantial value transaction based on materiality threshold as prescribed under LODR;
ix) passing of special resolution in respect of delisting or buy-back of shares; and
x) Any other provisions notified by SEBI in this regard from time to time.

Sunset Clauses:
SR Shares are required to be converted to ordinary shares on the 5th anniversary of listing (extendable by a further five years) or in the event of change of control or resignation of SR shareholder.

Fractional Rights Shares:
A fractional rights share refers to inferior voting rights shares. Existing listed companies are no longer allowed to issue fractional rights shares.

DISCLOSURE OF ENCUMBERANCES

In the context of concerns on promoters/companies raising funds from mutual funds and non-banking financial companies through structured obligations, pledge of shares and other complex structures, SEBI at its board meeting on 27 June 2019 approved the following amendments to the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011.

Earlier, the definition of "encumbrance" included pledge, lien or any such transaction. Pursuant to the amendment the definition of "encumbrance" has been widened to specifically include non-disposal undertaking or any covenant, transaction, condition or arrangement in the nature of encumbrance.

Additionally, pursuant to the amendment, promoters are now required to disclose the reasons for encumbrance if the combined encumbrance by the promoters and persons acting in concert crosses 20% of the total share capital in the company or 50% of their shareholding in the company. Further, promoters are required to declare annually that they along with persons acting in concert have not made any other encumbrance other than already disclosed. This declaration will be made to the audit committee of the company and to the stock exchanges.

INFORMAL GUIDANCE: WHETHER SEBI (ISSUE OF CAPITAL AND DISCLOSURE REQUIREMENTS) REGULATIONS, 2018 ARE APPLICABLE TO COMPANIES WHICH ARE SOLELY LISTED AT RECOGNISED REGIONAL STOCK EXCHANGE?

VC Corporate Advisors Pvt. Ltd. had approached SEBI for an informal guidance to clarify the applicability of the ICDR Regulations on behalf of its clients, which are companies whose equity shares are listed on the Calcutta Stock Exchange. Calcutta Stock Exchange is a recognised regional stock exchange which does not have nation-wide terminals.

As per Regulation 2(1)(dd) of the ICDR Regulations "listed Issuer" means an issuer whose equity shares are listed on recognised stock exchange having nation-wide trading terminals.

SEBI clarified that as per Regulation 3 of the ICDR Regulations which lays down the applicability of the ICDR Regulations, the companies proposing to raise funds by way of a preferential issue and/or bonus issue, even if listed on recognised stock exchange not having a nation-wide terminal, would have to comply with the provisions with respect to 'preferential issue' and 'bonus issue' as laid down under chapter V and Chapter XI of the ICDR Regulations, respectively.

INFORMAL GUIDANCE: WHETHER A LISTED ENTITY HAVING ONLY DEBT SECURITIES LISTED IS REQUIRED TO SUBMIT FINANCIAL RESULTS ON CONSOLIDATED BASIS UNDER REGULATION 52 OF SEBI (LISTING OBLIGATIONS AND DISCLOSURE REQUIREMENTS) REGULATIONS, 2018?

ONGC Videsh limited (**ONGC**) is in the business of exploration and production of oil and gas and other hydrocarbon related activities outside India. ONGC operates its business directly and through its various subsidiaries, associates and joint arrangements. ONGC has non-convertible debentures listed on National Stock Exchange (**NSE**) and does not have any equity shares listed on any of the stock exchanges in India.

Prior to the implementation of the Indian Accounting Standards (**Ind AS**), ONGC was submitting its half yearly financial results to NSE on both standalone basis and consolidated basis. However, post the implementation of Ind AS (i.e. April 01, 2016), ONGC only submitted half yearly financial results on standalone basis under Regulation 52 of the LODR Regulations. SEBI vide a circular dated November 27, 2015 had prescribed the format for submission of financial results and implementation of Ind AS by listed entities which have listed their debt securities and/or non-cumulative redeemable preference shares.

ONGC had approached SEBI for an informal guidance to clarify whether it could submit consolidated financial results over and above standalone financial results to the stock exchange in terms of Regulation 52 of the LODR Regulations.

Regulation 52 of the LODR Regulations requires the listed entity whose non-convertible debentures and/or non-convertible redeemable preference shares are listed to submit the half yearly unaudited financial results within 45 days from the end of the half year, or annual audited financial results within 60 days from the end of the financial year.

Neither Regulation 52 of the LODR Regulations nor the circular issued by the SEBI specified whether an entity which has subsidiaries is required to submit its financial results on only standalone basis, or on consolidated basis or both.

SEBI clarified that under Regulation 52(1) of the LODR Regulations, where a listed entity has only listed debt securities then that entity is only required to submit financial results on standalone basis.

RECOGNISED STOCK EXCHANGES WITH COMMODITY DERIVATIVES SEGMENT CAN TRADE IN FUTURE ON COMMODITY INDICES

SEBI has now permitted recognised stock exchanges with commodity derivative segment to introduce futures on commodity indices. The recognised stock exchanges desirous of trading in futures on commodity indices has to obtain prior approval of SEBI for launching such contracts.

The recognised stock exchange at the time of seeking approval has to submit at least 3 years data of the index constructed along with data on monthly volatility, roll over yield for the month and monthly return. Upon receiving the approval, the stock exchange has to publish the abovementioned data on its website before launch of the product.

SEBI has also given guidelines for the construction of the commodity indices and the product design for futures on commodity indices.

DISCUSSION PAPER: INFORMANT REWARD POLICY FOR INSIDER TRADING CASES

SEBI has been facing challenges in successfully prosecuting insider trading cases due to lack of direct evidence as insiders usually indulge in insider trading through a proxy to whom relevant information is communicated. Also, the details relating to the unpublished price sensitive information such as the precise time when the information was generated and when it became public and people who had access to it before it became public are absent.

As a step towards strengthening the mechanism for early detection and better enforceability SEBI has issued a discussion paper on an informant mechanism related to insider trading to mitigate challenges faced by SEBI.

The proposed mechanism will have a voluntary information disclosure form (**Disclosure Form**), through which the informant can submit credible, complete and original information relating to an act of insider trading. Informant will have to disclose the source of original information and will have to provide an indemnity to that effect as part of his undertaking.

If the informant wants to submit the Disclosure Form anonymously, he/she can do so by submitting it through an advocate who will act as an authorised representative of the informant.

Identity of the informant and the information provided will be protected by the Office of Informant Protection (**Office**) which will be an independent office. The Office will serve as a medium of exchange between the informant/legal representative and SEBI.

Informant will be rewarded 10 per cent of the money collected if the information provided leads to a disgorgement of at least Rs 5 crore. However, the reward will not exceed INR 1 crore or such higher amount as may be specified by the regulator, and such reward will be paid from the Investor Protection and Education Fund.

No employee will be discharged, terminated, demoted, suspended, threatened, harassed, or discriminated against, directly or indirectly for breaching the provisions of any terms and conditions of employment such as a confidentiality agreement, merely on account of filing the Disclosure Form or assisting the Office and every person associated with the securities markets, including listed companies and intermediaries, dealing with unpublished price sensitive information will incorporate in their code of conduct, suitable provisions to that effect.

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ACUITY LAW

Our co-ordinates:

Mumbai
C – 702, Marathon Nextgen Innova
Off Ganpath Rao Kadam Marg
Lower Parel, Mumbai – 400 013

Delhi
D-17, Lower Ground Floor, Lajpat Nagar,
Part-3, New Delhi-110 024, India

Bangalore
C/o Wework, 9th floor, RMZ Latitude Commercial bldg,
Bellary Road, Hebbal, Bangalore-560024

www.acuitylaw.co.in

al@acuitylaw.co.in