

ACUITY LAW

**SECURITIES  
LAW NEWSLETTER**

MAY 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](http://acuitylaw.co.in) or write to us at [al@acuitylaw.co.in](mailto:al@acuitylaw.co.in)

## INTRODUCTION

This newsletter covers key updates about the developments in Indian securities law during the month of May 2019. We have summarized the key regulatory developments including an order passed by the market regulator on the National Stock Exchange co-location case; circulars issued by Securities and Exchange Board of India on (a) framework for innovation sandbox, (b) accreditation of investors to innovators growth platform, and (c) enhanced disclosure norms for listed debt securities by debenture trustees; and discussion papers issued by Securities and Exchange Board of India on (a) review of rights issue process, and (b) regulatory sandbox framework for financial institutions.

Please see below the summary of the relevant regulatory developments.

## NATIONAL STOCK EXCHANGE CO-LOCATION CASE

**Matter:** Securities and Exchange Board of India Vs. National Stock Exchange & Ors.

**Order date:** 30 April 2019

### Summary:

In the National Stock Exchange (**NSE**) co-location case, Securities and Exchange Board of India (**SEBI**) had initiated enforcement action against various entities following allegations that the exchange had given some traders preferential access to its co-location facility. Co-location is a facility provided by NSE where trading members can place their servers in the exchange's data centre, in order to get faster access to the price feed, helping in swift execution of trades. The accused entities in the case were probed for rigging the system and for providing preferential access to certain brokers by giving them access to the backup servers in the co-location facility.

Pursuant to the probe it was discovered that certain brokers were able to undertake high-frequency trades for four years between 2010 and 2014 as a result of the highspeed access. As a result of preferential access, these brokers had enriched themselves and their clients.

In this matter SEBI on 30 April 2019 directed the NSE to 'disgorge' Rs. 6248.9 million with 12 percent per annum interest. The regulator also barred the exchange from the securities market for six months. This meant that NSE could not access the capital market for six months. SEBI also found the two former managing directors of NSE guilty in the case and directed them to disgorge 25% of their salary drawn for the relevant financial years. The disgorgement amount had to be deposited in the Investor Protection and Education Fund.

However, Securities Appellate Tribunal has granted interim relief to the respondents in the present case by putting a stay on the effect and operation of the order passed by SEBI and will take up all the appeals in this case on 22 July 2019 for final disposal.

## FRAMEWORK FOR INNOVATION SANDBOX

SEBI vide circular dated 20 May 2019 announced the framework for 'innovation sandbox'. Under the innovation sandbox, FinTech firms/entities not regulated by SEBI (**Participants**) will be provided a testing environment for offline testing of proposed innovative solutions on products, services, and/or solutions for the securities and commodities market in India. Under the innovation sandbox framework, the Participants will be provided market related data such as trading and holding data to test their innovations effectively prior to introduction of the innovation in the live market.

The framework classifies the features and structure of innovation sandbox broadly into design, legal and administrative categories, and lays down eligibility criteria for the participants. The key aspects of the framework for the innovation sandbox are discussed below:

**Eligibility:** The Participants will have to demonstrate that the solution offering identifiable benefits to consumers, the capital market and the economy, cannot be developed without testing in the innovation sandbox. Further, the participant will have to provide testing plans, with objectives, parameters and success criteria, post-testing plan and cyber-security compliance as per SEBI's cyber security guidelines.

**Data Access:** The Participants will be given access, on a strictly confidential basis, to historical and anonymized data including data to episodic market events in a phased manner to test and improve their innovations. The indicative data which may be included for this purpose is depositories data (holding data, know your customer data), stock exchange data (transaction data such as order log and trade log) and registrar and transfer agent data (mutual fund transactions data).

**Required Infrastructure:** The Participants will be provided the data through application program interface. Further, the Participants will have access to virtual machines with configurations similar to live markets for testing their innovations on the basis of the data provided.

**Other matters:** It is proposed that the Participants should be set up as a non-profit entity and permitted to enter the innovation sandbox on the basis of rule based self-assessment process. Also, adequate protective measures will be put in place to protect the stakeholders, prevent any misuse of data provided to Participants, protect the Participants intellectual property rights and ensure compliance of regulations by the Participants.

**Administration:** The governing body will supervise the operation of the innovation sandbox and is proposed to comprise of representatives of stock exchanges, depositories and registrar and share transfer agents.

## ACCREDITATION OF INVESTORS TO INNOVATORS GROWTH PLATFORM

SEBI vide circular dated 22 May 2019 has announced the framework for accreditation of investors to the innovators growth platform (**Platform**). The Platform is a trading platform for listing and trading of specified securities of issuers which are 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.

**Eligibility criteria for accreditation of investors:** Investors who hold investment in an issuer company comprising of at least 25% of the pre-issue capital of the issuer company are eligible for accreditation to the Platform. In addition, the monetary threshold required to be satisfied by an investor for accreditation to the Platform is provided below: (i) for individuals: gross annual income of INR 5,000,000 and liquid net worth of INR 50,000,000; and (ii) for body corporates, net worth of INR 250,000,000.

**Accreditation process:** The investor will have to apply for accreditation through an application with documents as listed in the circular to the stock exchange or depositories. While the stock exchanges can use the services of brokers and depository participants, the stock exchanges and depositories will be responsible for verification and maintenance of the investor data. The accreditation will be valid for 3 years from the date of issuance. SEBI has directed the stock exchanges and depositories to implement the procedure for accreditation within 45 days from the date of the circular.

When a company applies for listing on the Platform, the merchant bankers must ensure due diligence regarding the eligibility of accredited investors and that their holding in the company desirous of listing on the Platform, is in accordance with Regulation 283(1) of SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018.

### SEBI NOTIFIES ENHANCED DISCLOSURE NORMS FOR LISTED DEBT SECURITIES BY DEBENTURE TRUSTEES

SEBI vide circular dated 27 May 2019 has issued guidelines after taking into consideration the public comments, with a view to further secure the interests of investors in listed debt securities, enhance transparency and to enable debenture trustees to perform their duties effectively and promptly.

The guidelines are as follows:

1. In order to increase transparency, debenture trustees will be required to display on their website the following:
  - i. the nature of compensation arrangement with its clients including the minimum fee to be charged (in absolute terms or as a percentage of the issue size) and factors determining the same.
  - ii. the ISIN wise details of interest/redemption due to the debenture holders in respect of all issues during the financial year within 5 working days of start of financial year and update such details for any new issues handled during the financial year within 5 working days of closure of the issue.
  - iii. the status of payment ISIN wise against such issuers not later than 1 day from the due date. In case the payment is made with a delay by the issuer, debenture trustees will update the calendar specifying the date of such payment, with a remark '*delayed payment*'.
2. In order to enable debenture trustees to keep their records updated and to communicate effectively with the debenture holders, the registrars to an issue and share transfer agent or issuer will have to forward the details of debenture holder to the debenture trustee at the time of allotment and periodically by the seventh working day of each month. This provision is especially relevant in case default provisions are triggered for the issuance.
3. Additional covenants required to be included in the term sheets executed on or after 7 May 2019 are:
  - i. Additional interest on payment default: In case of payment default of interest and/or principal on due dates, additional interest of at least 2% p.a. over the coupon rate will be payable by the issuer.
  - ii. Delay in Listing: In case of delay in listing of the debt securities beyond 20 days from the deemed date of allotment, the issuer will pay penal interest of at least 1% p.a. over the coupon rate from the expiry of 30 days from the deemed date of allotment till the listing of such debt securities to the investor.

### DISCUSSION PAPER ON REVIEW OF RIGHTS ISSUE PROCESS

SEBI on 21 May 2019 released a discussion paper on review of rights issue process. SEBI had enabled rights issue through the fast track route, subject to certain conditions, cutting down significantly on the timelines, however, SEBI is further exploring ways to make the rights issue process more efficient.

Currently, issuers perceive a higher exposure to price risk due to current rights issue process while investors expect allotment and listing timelines to be shortened. The current process of trading of rights entitlement, which is settled physically with low liquidity, is an area which needs to be addressed too.

SEBI in this discussion paper has evaluated means to:

- (i) reduce time between announcement of terms of the issue and issue closing thereby reducing price risks, and
- (ii) make the application and allotment process more efficient by using the banking and depository infrastructure and provide issuers with an efficient mechanism for raising funds, and to streamline the process, reduce post issue timeline for rights issues and methodologies associated with rights issue fund raising process.

SEBI has proposed the following changes in the discussion paper:

- (i) to reduce the notice period under Regulation 42 of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 to 3 clear working days (instead of 7 clear working days), and the requirement to determine issue price prior to record date may continue.
- (ii) issuers may intimate stock exchanges before issue opening about dispatch completion, which would be notified to shareholders / investors through the corporate announcements' module on the exchange websites instead of publishing an advertisement.
- (iii) moving to electronic modes of receiving entitlements, processing, payment and settlement in a rights issue. This will make the process more transparent and efficient. All investors would be required to use applications supported by blocked amount i.e. ASBA facility as a payment mode, this will enable faster completion of the post issue process.

## **'REGULATORY SANDBOX' FRAMEWORK FOR FINANCIAL INSTITUTIONS**

SEBI on 28 May 2019, released a discussion paper on framework for regulatory sandbox to grant certain facilities/flexibilities to SEBI regulated financial institutions and enable them to experiment with financial technology solutions in a live environment. The regulatory sandbox is a live, testing environment where new products, processes, services and business models can be deployed on a limited set of eligible customers for a specified time period with certain relaxations in the extant SEBI regulations and guidelines.

It is proposed that all market participants registered with SEBI under section 12 of the SEBI Act, 1992, will be eligible for testing within the regulatory sandbox. However, SEBI may consider permitting financial technology start-up, firms and other entities that are not regulated by SEBI, to participate in the regulatory sandbox. Key aspects of the discussion paper are discussed below:

**Exemption:** The market participants who want to participate in the regulatory sandbox can make an application for exemption / relaxation from relevant provisions of SEBI regulations that they feel are hampering their innovations or are acting as barriers to entry of new products.

**Eligibility:** The market participants' solution should be truly innovative or significantly different from existing offerings. The applicant should demonstrate that the solution cannot be developed without relaxing certain regulations within the sandbox. The solution is required to be tested offline for a limited period. The applicant must show well developed testing plans with clear objectives, parameters and success criteria. The applicant should share a proposed sandbox exit and transition strategy to demonstrate his intentions of deploying the solution in India on a broader scale.

**Potential Risk Mitigates:** The applicant is required to follow appropriate disclosure, protection and compensation requirements related to their users agreed upon, on a case-by-case basis.

**Application and Approval Process:** A rolling approach will be followed wherein the applicant can apply anytime for participation in the regulatory sandbox. If the applicant is a suitable participant for the sandbox and the project meets the eligibility criteria, it can proceed to submit the sandbox application form signed by the chief executive officer (CEO) of the applicant or officer duly authorized by the CEO or registered individual, to SEBI. At the "Application Stage", SEBI will review the application and inform the applicant of its potential suitability for a sandbox within 30 working days from the submission of the complete application. At the "Evaluation Stage", SEBI will work with the applicant to determine the specific regulatory requirements and conditions (including test parameters and control boundaries) to be applied to the proposed solution in question. The applicant will be required to inform during the "Testing Stage" to the users that the solution is operating in a sandbox and disclose the key risks associated with the financial service. The proposed duration of the sandbox is nine months with a maximum extension (upon request) of three months.

**Revocation of the Approval:** SEBI can revoke an approval to participate at any time before the end of the testing period by giving the participant 30 days' notice in writing of its intention to revoke the approval.

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