REGULATORY FRAMEWORK

GOVERNMENT PLANS TO EASE, SCRAP FDI SECTORAL LIMITS

The government is likely to either increase or scrap the foreign direct investment (FDI) limit in sectors where it is set at less than 100%, in an ambitious reform to encourage foreign investors to loosen their purse strings and thus step up FDI flows to rein in current a/c deficit The government has noticed that FDI caps provide an opportunity for Indian promoters to make quick money but puts unnecessary hurdles in the way of foreign direct investment, which is considered the most stable form of capital inflow. A comprehensive revamp of the FDI regime was thus debated in the run-up to the budget in the wake of mounting concerns over record-high current account deficit. Current account deficit was 4.6% of GDP in April-September 2012 and could be as high as 5% for the year ended March 31, 2013.
Sectors such as banking and telecom, where 74% FDI is allowed, are high on the review list. Some changes may also be announced in the upcoming annual review of the investment policy on April 1. A discussion paper put out by DIPP in 2011 had first suggested getting rid of caps, but the idea gained currency after the Reserve Bank of India (RBI) backed the idea. The foreign direct investment policy currently mandates equity caps at broadly four levels — 26%, 49%, 51% and 74%.

(**Source**: Economic Times dated 11th March, 2013)

REGULATIONS FOR ISSUANCE AND LISTING OF NON-CONVERTIBLE REDEEMABLE PREFERENCE SHARES

SEBI Board approved the SEBI (Issue and Listing of Non-Convertible Redeemable Preference Shares) Regulations, 2013 thus providing a comprehensive regulatory framework for issuance and listing of non-convertible redeemable preference shares. Considering the risks involved in these instruments, the SEBI Board has proposed certain requirements like minimum tenure of the instruments (three years), minimum rating ("AA-" or equivalent) etc. have been specified in case of public issuances. For listing of privately placed non-convertible redeemable preference shares, minimum application size for each investor has been fixed at Rupees Ten Lakhs.

As per Basel III norms, Banks can issue non-equity instruments such as Perpetual Non-Cumulative Preference Shares and Innovative Perpetual Debt Instruments, which are in compliance with the specified criteria for inclusion in Additional Tier I Capital. The proposed Regulations shall, mutatis mutandis, be applicable to aforesaid instruments issued by banks, subject to compliance with the provisions of Companies Act, 1956 or/ and any other applicable laws and such other conditions that may be specified by SEBI.

(**Source**: SEBI Board Meeting No. dated 8th March, 2013)

SCHEME OF ARRANGEMENT UNDER THE COMPANIES ACT, 1956 – REVISED REQUIREMENTS FOR THE STOCK EXCHANGES AND LISTED COMPANIES

SEBI has revised the requirements of stock exchanges and listed companies with respect to filing of scheme of arrangement.
Prior to this circular, pursuant to a scheme of reconstruction or merger/ de-merger/ amalgamation being sanctioned by the High Court under Sections 391-394 and Sections 101 of the Companies Act, 1956,

listed companies desirous of getting their equity shares listed after merger/demerger/ amalgamation etc. were required to seek an exemption from SEBI.

SEBI on a review of the past indiscretions by certain entities is of the view that granting listing permission or exemption from the requirements of Securities Contracts (Regulation) Rules, 1957 (**SCRR**) would be detrimental to the interest of minority shareholders and also at the same time, if listing permission or such an exemption is delayed or denied, it would add to the uncertainty and would deprive shareholders of an exit opportunity.

Therefore, in order to avoid such situations, pursuant to the aforementioned circular, SEBI has accordingly revised the requirements. Some of the salient features of the said circular are as under:

(i) **Obligations of listed companies**: Listed companies are required to (a) File the draft scheme with the stock exchanges; (b) Place before its Audit Committee a Valuation Report from an Independent Chartered Accountant; (c) Designate a stock exchange with nationwide terminals for the purpose of co-coordinating with SEBI; (d) Circulate an observation letter with the EGM notice to all its shareholders seeking the approval of the scheme; and (e) bring the same to the notice of the High Court at the time of seeking approval of the scheme.

(ii) **Obligations of stock exchanges**: Stock exchange(s) are *inter-alia* required to (a) forward the scheme (along with the documents mentioned at (i) above) to SEBI within the prescribed time frame; (b) process the draft scheme filed by the listed company and forward their Objection/ No objection certificate to SEBI within the prescribed time frame; and (c) issue Observation Letter to the listed company after suitably incorporating the comments received from SEBI.

(iii) **Processing of the Draft Scheme by SEBI**: Upon the receipt of the documents from the stock exchange, SEBI is required to endeavor to process and provide comments on the draft scheme within the prescribed time frame.

(iv) **Disclosure on the Website**: Within the prescribed time frame, the listed company and the chosen stock exchange need to disclose on their respective websites the draft scheme and all the documents along with the Observation letter (as and when issued)

(v) **Redressal of Complaints**: The circular sets out the process for redressal of complaints by SEBI and the designated stock exchange.

(vi) **Shareholders' approval through special resolution passed through postal ballot and e-voting:** Listed companies are required to ensure that the scheme which is filed with the High Court *inter-alia* provides for obtaining shareholders' approval through special resolution passed through postal ballot and e-voting and the explanatory statement served on the shareholders in relation to such resolution sets out all the material facts.

The revised requirements will be applicable to all listed companies which, on the date of this Circular have not submitted the draft scheme to the High Court. It has also been clarified that the revised requirements will also be applicable to listed companies that have submitted the draft scheme with the stock exchanges and have already received approval thereon but have not yet submitted to the High Court, therefore such companies will be required to resubmit the scheme in accordance with the requirements of this circular. Pursuant to this circular, SEBI Circular No. SEBI/CFD/SCRR/01/2009/03/09 dated September 03, 2009 stands rescinded.

Looked at from the perspective of shareholders, the revised requirements are robust, however when looked at from the perspective of listed companies, the revised requirements may require multiplicity of shareholders approval, time consuming processes, etc. SEBI has brought about revised requirements with clear focus on protection of interest of minority shareholders. Introduction of requirements such as report from audit committee, observations from SEBI, full disclosures of filings with stock exchanges on website of listed companies and stock exchanges have paved way for more informed decision for shareholders. Requirement for approval of the Scheme of Arrangement by 2/3rd of public shareholders would give a real representation to minority shareholders in the decision making of listed companies which may be mere relevant once the Companies Bill, 2012 is enacted. This Circular has come into force.

(**Source**: SEBI Circular No. CIR/CFD/DIL/5/2013 dated February 4, 2013)

NO ESOS/ESPS SHALL INVOLVE ACQUISITION OF SECURITIES FROM THE SECONDARY MARKET

SEBI vide a circular dated January 17, 2013 has inserted Regulation 22B prohibiting the listed entities from framing any employee benefit schemes involving acquisition of own securities from the secondary market in view to address the concerns over acquisition of shares by employee welfare trusts from the secondary market for manipulating the price of the securities.
In respect of those companies, which have already framed and implemented before the date of this circular any employee benefit schemes involving dealing in the securities of the company, which are not in accordance with SEBI (ESOS and ESPS) Guidelines, 1999 it has been decided that:-

i. such companies will be required to inform the details of their schemes to the Stock Exchanges within 30 days from date of this circular, in a prescribed format and to disseminate the said information on their website.
ii. such companies shall align any existing employee benefit schemes with SEBI (ESOS and ESPS) Guidelines on or before June 30, 2013.

(**Source:** SEBI Circular No. CIR/CFD/DIL/3/2013 dated January 17, 2013)

GUIDELINES FOR ENABLING PARTIAL TWO-WAY FUNGIBILITY OF INDIAN DEPOSITORY RECEIPTS (IDRS)

Securities and Exchange Board of India ("SEBI"), vide circular No. CIR/CFD/DIL/10/2012 dated August 28, 2012, had prescribed the framework for redemption of IDRs into underlying equity shares. The circular had also provided for partial fungibility of IDRs in a financial year to the extent of 25% of the IDRs originally issued. In order to encourage more number of foreign companies to issue IDRs in the Indian market and also to enable the investors to take informed investment decision, it has been decided to provide a detailed roadmap and guidelines for the future IDR issuances as well as for the existing listed IDRs.

All the IDRs shall have partial two-way fungibility. The partial two-way fungibility means that the IDRs can be converted into underlying equity shares and the underlying equity shares can be converted into IDRs within the available headroom.

I. Guidelines for fungibility of future IDR issuance

- IDRs shall not be redeemable into underlying equity shares before the expiry of one year period from the date of listing of IDRs.
- After completion of one year period from the date of listing, the issuer shall, provide two-way fungibility of IDRs.
- IDR fungibility shall be provided on a continuous basis.
- The issuer shall provide said fungibility to IDR holders only in prescribed manners, provided that the option once exercised and disclosed to public cannot be changed without specific approval of SEBI.
- All the IDRs that have been applied for fungibility by the holder shall be transferred to IDR redemption account at the time of application. (Also Applicable to **existing listed IDRs)**
- The Issuer may receive requests from the holders of underlying shares and convert these into IDRs subject to the Headroom available and the guidelines prescribed by SEBI & RBI. (Also Applicable to **existing listed IDRs)**
- In case of option of converting the IDRs into underlying equity shares, the issuer shall disclose the range of fixed/variable costs in percentage terms, and ensure that all the costs together shall not exceed 5% of the sale proceeds. (Also Applicable to **existing listed IDRs)**
- Available Headroom and significant conversion/ reconversion transactions shall be disclosed by the issuer on a continuous basis. (Also Applicable to **existing listed IDRs)**

II. Guidelines for fungibility of existing listed IDRs

- After completion of one year period from the date of issue of IDRs, the issuer shall, every year provide redemption/conversion of IDRs into underlying equity shares of the issuer of up to 25% of the IDRs originally issued. The Issuer shall also invite expression of interest from IDR holders at least one month before the implementation.
- The issuer shall provide the said fungibility to IDR holders only in the prescribed ways.
- The periodicity for IDR fungibility shall be at least once every quarter. The fungibility window shall remain open for the period of at least seven days.
- Total number of IDRs available for fungibility during one fungibility window shall be fixed before the opening of the window. Re-issuances of IDRs during the fungibility window, if any, shall be considered for computation of Headroom only at the time of next cycle of fungibility.
- In case of requests for conversion in excess of the limit available, the manner of accepting IDRs for conversion/ redemption or shares for re-issuance shall be on proportionate basis.

- A reservation of 20% of the IDRs made available for redemption/conversion into underlying equity shares in the fungibility window shall be provided to Retail Investors
- Existing issuers shall provide the option of redemption/ conversation within three months of notification of these guidelines.
- The existing issuer of IDR may exercise the option of using the guidelines available for the new issuers as referred above from the anniversary of the date of listing of their IDRs after the issuance of this circular or from any of the subsequent quarters thereafter. The said option, once exercised, will not be reversed.

The issuer shall lay down the detailed procedures while taking into consideration the above broad guidelines in addition to other norms specified by SEBI and RBI, from time to time. With issuance of this circular, SEBI circular No: CIR/CFD/DIL/10/2012 dated August 28, 2012 shall become effective and SEBI circular No: CIR/CFD/DIL/3/2011 dated June 03, 2011 would stand rescinded.

(Source: SEBI Circular No. CIR/CFD/DIL/6/2013 dated March 1, 2013)

SEBI ADJUDICATION ORDER: "PERSONS ACTING IN CONCERT"

In the matter of Bank of Rajashthan Ltd (BoR) vs. Pravin Tayal and Ors.

Facts: Pursuant to the RBI Guidelines on Ownership and Governance in Private Sector Banks dated February 28, 2005, the promoters of BoR were required to reduce their shareholding in the company. While the promoters did in fact reduce their stake in the company, certain other companies fronting for the promoter group were acquiring BoR shares in parallel, and no disclosures were made regarding those acquisitions either under the listing agreement or the SEBI Takeover Regulations. Such purchaser entities had contact details similar to that of BoR's promoters; and there were common directorships between the promoter group and the acquiring entities.

Key Issues: Whether the several entities that engaged in the sale and purchase of shares of BoR were interconnected and hence persons acting in concert for purpose of the Takeover Regulations. The test applied by the adjudicating officer after analyzing the various relationships between the entities and the trades among them is as follows:
In view of the above, I find that connections/ relations have been established on the basis of common directors, common addresses, fund transfers, off market transfer of shares, and the submission of the Noticees is devoid of merit. Accordingly, I hold that the Promoter, Tayal, Yadav and Silvassa group were PACs.

Order: The order imposes a heft penalty on 118 entities that traded in shares of BoR for violation of the provisions of the SEBI Takeover Regulations and the SEBI Regulations on Fraudulent and Unfair Trade Practices.

(Source: SEBI Adjudicating Order No. BM/AO/8-125/2013 dated February 14, 2013

RBI DRAFT GUIDELINES: REVIEW OF PRUDENTIAL GUIDELINES ON RESTRUCTURING OF ADVANCES BY BANKS AND FINANCIAL INSTITUTIONS

The Reserve Bank of India (RBI) has issued draft guidelines on "Review of Prudential Guidelines on Restructuring of Advances by Banks and Financial Institutions" that follows from the recommendations of the working group on the subject under the chairmanship of Mr. B. Mahapatra.
The draft guidelines contain several technical details regarding prudential norms on income recognition, asset classification and provisioning as well as on substantive and procedural issues pertaining to the restructuring process itself. They have been sub-divided as:

- Doing Away with Regulatory Forbearance
- General Provision on Restructured Standard Accounts
- Provision for Diminution in the Fair Value of Restructured Advances
- Criteria for Upgradation of Account Classified as NPA on Restructuring
- Benchmarks on Viability Parameters
- Viability Time Period
- Incentive for Quick Implementation of Restructuring Package
- Roll over of Short-Term Loans
- Asset Classification Benefits on Restructuring of Infrastructure Project Loans – Jurisdictional Limits
- Promoters' Sacrifice
- Conversion of Debt into Equity / Preference Shares
- Right of Recompense
- Personal Guarantee of Promoters

As far as classification is concerned, the current system of regulatory forbearance will be continued until April 1, 2015, whereby "standard accounts are allowed to retain their asset classification and [non-performing asset (NPA)] accounts are allowed not to deteriorate further in asset classification on restructuring". However, from April 1, 2015, this would change and classification benefits available on restructuring may be withdrawn.
As for the restructuring process itself, the effort seems to be to streamline and tighten the process further. Only those cases where the viability of the unit (within a relatively shorter period of time) is guaranteed may be taken up for restructuring. Greater contribution is sought from promoters for restructurings so that they retain a "skin in the game" – these could be in the form of promoter's sacrifice and additional funding as well as personal guarantees.
Overall, the guidelines seem to be more prescriptive in terms of regulating asset provisioning and corporate debt restructuring. While they place filters to ensure that only the most deserving cases will be subject to turnarounds, greater regulatory intervention (as opposed to forbearance) may reduce the incentive to companies and lenders to pursue restructuring as an option if the process becomes too cumbersome.

(Source: RBI Draft Notification No. RBI/2012-13/ DBOD.BP.BC.No. /21.04.132/2012-13 dated January 31, 2013)

TIME PERIOD FOR INITIAL OFFERING AND ALLOTMENT OF UNITS OF MUTUAL FUND SCHEME ELIGIBLE UNDER RAJIV GANDHI EQUITY SAVINGS SCHEME, 2012 (RGESS)

With respect to Mutual Fund scheme eligible under RGESS, which is a tax-saving scheme notified by the Government of India on November 23, 2012, it has been decided that –
The maximum period for which initial offering of Mutual Fund scheme eligible under RGESS shall be open for subscription, is extended from the existing stipulation of fifteen days to thirty days. Further, for Mutual Fund scheme eligible under RGESS, the period within which Mutual Fund/ AMC should allocate the units, refund money and issue statements of accounts, is extended from the existing requirement of five working days from the closure of the initial subscription to fifteen days from the closure of the initial subscription. This circular has come into force.

(Source: SEBI Circular No. CIR/ IMD/ DF/02/2013 dated February 06, 2013)

LIQUIDITY ENHANCEMENT SCHEMES (LES) FOR ILLIQUID SECURITIES IN EQUITY CASH MARKET

It is now permitted for stock exchanges to introduce LES to enhance liquidity of illiquid securities in their Equity Cash market. LES may be introduced in any of the following securities:

Securities having a mean impact cost greater than or equal to 2% for an order size of Rs.1 lakh, where mean impact cost of the security on the stock exchange is calculated over the past 60 trading days and

Securities introduced for trading in the "permitted to trade" category.

LES may be continued till such time as the security achieves mean impact cost of less than 2% for an order size of Rs.1 lakh on the stock exchange during the last 60 trading days. Discontinuation of LES for any security can be done after advance notice of 15 days. Stock exchanges can also re-introduce LES on a security. In case any stock exchange introduces LES on securities eligible under this circular, other stock exchanges may also introduce LES in the same securities even if those are not eligible on their stock exchange. Such LES of other stock exchanges shall not be continued beyond the period of LES at the initiating stock exchange.

The incentives under LES shall be transparent and measurable. These may be either (a) Discount in fees, adjustment in fees in other segments or cash payment or (b) Shares, including options and warrants, of the stock exchange.

The Stock Exchange shall submit half-yearly reports on the working of its LES for review of SEBI and it shall ensure that the LES complies with all the relevant rules, regulations and laws.

Further this circular shall not be applicable to securities listed on SME Platform or SME Exchange, and the conditions specified in SEBI circular SMDRP/Policy/CIR-04/2000 dated January 20, 2000 shall not be applicable for the LES introduced pursuant to this circular. SEBI circular CIR/DNPD/5/2011 dated June 02, 2011 stands modified by this circular.

(Source: SEBI Circular No. CIR/MRD/DP/05/2013 dated February 08, 2013)