MMJCINSIGHTS

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Can Equity Shares be converted into Redeemable Preference Shares??

I. Introduction:

- Share Capital of a Company may comprise of two kinds of capital Section 43 of Companies Act 2013 ("the Act") states that "The share capital of a company limited by shares shall be of two **kinds**, namely:—

  (a) equity share capital—

  (i) with voting rights; or

  (ii) with differential rights as to dividend, voting or otherwise in accordance with such rules as may be prescribed; and

  (b) preference share capital"

- Conversion of preference share capital into equity share capital is quite common. But then whether vice versa, i.e., conversion of **equity** share capital **into preference** share capital **is possible**? **If yes, then how? If no, then why?** We shall deliberate on these questions in this article.

II. Difference between equity shares and preference shares:

- The major point of difference between equity share and preference share pertains to voting rights and preference in distribution of dividends and repayment of capital.
- **Voting rights -** As per section 47(1) of the Act, every member holding equity share capital has a right to vote on every resolution placed before the company; whereas as per section 47(2), every member holding preference share capital therein has a right to vote only on resolutions placed before the company which directly affect the rights attached to his preference shares and, any resolution for the winding up of the company or for the repayment or reduction of its equity or preference share capital.
- **Preference over equity shares** – As per the definition of "preference share capital" in section 43, the preference shares would carry a preferential right with respect to payment of dividend and repayment, in the case of a winding up or repayment of capital.
- As per second proviso to **sec 47(2)** if dividend in respect of a **class of preference shares** has not been paid for a period of two years or more, **such class of preference shareholders** shall have a right to vote on all the resolutions placed before the company."

III. Interplay between the words "kinds" and "classes":

- Some examples where the word "class" has been referred are:-
    - In second proviso to section 47(2) which speaks about when a particular class of preference shares acquire voting rights on all resolutions placed before company;
    - In section 48 which speaks about variation of rights attached to the shares of any class;
    - In section 49 which speaks about making calls on shares of a class;
    - In section 88 which speaks about register of members indicating separately **for each class of equity and preference shares.**
- However, section 43 which explains the meaning of equity share capital and preference share capital uses the words "kinds" and not "class".
- So a question arises that whether "classes" and "kinds" mean same thing Or do they mean different things?
- On harmoniously reading sec 43, sec 48, sec 88 and other sections where the word 'classes of shares' is ued, it can be inferred that there are only two kinds of shares – equity shares and preference shares.
- Within these kinds of shares, there can be classes of shares having different rights.

IV. Variation of rights attached to shares of any class:

- Under sec 48, variation of rights of class of shares is possible after following the process elaborated in sec 48.
- The phrase *'variation of rights of class of shares'* will include variation in rights of classes of preference shares and classes of equity shares too.
- This means if there is only one class of shares in each kind of shares OR even if there are multiple classes of shares in each kind of shares, the rights attached to them can be varied by following the process u/s 48.
- Here a question arises that **can such variation of rights** of one or multiple classes of shares **be done** (under sec 48) **to the extent that it crosses the boundary of basic character (kind of) shares to which it belongs to**?

A. Conversion from redeemable preference shares to convertible preference shares:

- **Section 48 quotes** that "*Where a share capital of the company is divided into different classes of shares, the rights attached to the shares of any class may be varied* ***with the consent in writing of the holders of not less than three-fourths of the issued shares of that class*** *or by means of a special resolution passed at a separate meeting of the holders of the issued shares of that class"*

- This shows that variation of rights **under sec 48 does not require consent of each shareholder**. It can be varied with the **consent of requisite majority**.
- If company wants to **convert redeemable preference shares to convertible preference shares**, it can be done only with the consent of each preference shareholder and also after passing special resolution under section 62(1)(c) and after complying with Section 42 and complying with the Rules relating to section 42 and 62(1)(c).

B. Conversion from equity shares to redeemable preference shares:

- When it comes to **conversion of equity shares into preference shares**, it is not specifically mentioned under any provision of the Companies Act 2013.
- Hence a question arises that **can such conversion be done with the consent of each equity shareholder** as there is no requisite majority prescribed for this matter under any section?
- View on conversion of equity shares into redeemable preference shares are very diverse.
- One view can be that conversion of shares from one kind to another kind leads to capital extinguishment of the former kind of shares, and hence the same can only be done through reduction of capital with the approval of the Tribunal.
- Another view can be it need not be equated to reduction as only the nature of share capital changes without any financial outlay (at the time of conversion).

V. Recent NCLT Order in this matter:

- The National Company Law Tribunal (**NCLT**) Mumbai Bench in the *Scheme of Arrangement and Amalgamation of Protrans Supply Chain Management Private Limited and Ors*.1 … ('Transferor Company I'), Ag-Vet Genetics Private Limited … (Transferor Company II) with **Baramati Agro Limited** … (Transferee Company') and their respective shareholders. **NCLT Mumbai order dated 20 September 2021,** has brought clarity over this subject matter and has provided corporates with a structured exit and increased flexibility in reorganising capital.
- In this case, NCLT allowed conversion of equity shares of Transferee company (Baramati Agro Limited) into preference shares under a Scheme of Arrangement. In the said case the transferee company had 21,675 Class A equity shareholders, of which 21,000 shareholders held small amount of equity shares. These small shareholders were regularly requesting for dividend and had also insisted on redemption of their investments within a fixed timeframe.
- In light of this, as a part of a Scheme of Arrangement where two other companies were getting merged into this company, the Scheme proposed conversion of certain Class A equity Shares of transferee

Co into 9% non-cumulative optionally convertible redeemable preference shares of rupees 10 each.

- The Scheme was duly approved through corporate resolutions, and an undertaking was furnished by the parties that they would comply with all NCLT directions, Companies Act 2013 and applicable accounting standards. As such the scheme was not objected to by any stakeholder (such as Official Liquidator, Income-tax department), except by the Registrar of Companies Pune. The two *main grounds against conversion:*
    (i) *conversion is not permissible as value, terms, and rights of equity shares were different than preference shares, and*
    (ii) *as shares are different, an equivalent conversion ratio for preference shares is not possible.*
- The NCLT noted that a **conversion from one kind to another is reorganisation of share capital** which is **expressly allowed under Section 61 of Companies Act, 2013**. Section 61 allow companies to pass necessary resolutions for increasing authorised share capital, consolidation and division of existing shares into larger value shares, conversion of fully paid share to stock and vice versa, sub-division of existing shares to smaller amounts, and cancellation of shares, subject to authorisation in articles.
- **Section 230** of Companies 2013 **allows a scheme** of compromise or arrangement **to be in the form of reorganisation of share capital**, and thus, a scheme could comprise of increase, consolidation, sub-division, reduction or conversion of shares. In any event, **arrangement has to be given wide scope** as well settled in several cases.
- NCLT ruled in this case that the scheme was fair and reasonable and allowed the proposed conversion as part of the scheme. No adverse observations or objections were raised by Official Liquidator or Income-Tax department plus all procedural compliances under Companies Act 2013 were fulfilled.
- Hence **NCLT permitted the conversion of equity shares into redeemable preference shares in Baramati Agro Limited**

VI. Other Supreme Court & High Courts' judgements quoted by NCLT in this case:

- NCLT quoted a judgement of ***The Supreme Court in Rajendra Prasad Gupta v. Prakash Chandra Mishra and Ors. SLP No 984 of 2006*** has held that *"Courts are not to act upon principal that every procedure is to be taken as prohibited unless it is expressly provided for by the Code, but on the converse principal that **every procedure is to be understood as permissible till it is shown to be prohibited by the law**. As a matter of general principle, **prohibition cannot be presumed**".*

- NCLT also quoted a judgement of ***Hon'ble Bombay High Court in Vasant Investment Corporation Ltd CA No 178 of 1978*** wherein it was held that *"if a scheme is proposed which involves a restructuring of the capital of the company – as in a case where the rights of the various shareholders are sought to be altered – it can also be said that under the existing memorandum and articles of association of the company, the rights of the shareholders are fixed in a certain way and to change them would involve sanctioning an act which is ultra vires the memorandum and articles of association. Strictly speaking, such an act may be considered as ultra vires. But, in fact, the very purpose of a scheme of reconstruction is to make suitable alterations in the structure of the company to enable it to function. A scheme, therefore, which contains such ultra vires provisions can be sanctioned, and is in fact, sanctioned in a number of cases."*

VII. Conclusion:

- To conclude following facts are required to be paid attention to:-
  (a) Company needs to have some equity share capital, then only it can have preference capital. **Entire equity share capital cannot be converted into preference capital, although some part of equity share capital can be converted** into preference share capital
  (b) Since there is no express provision in this regard, **it will require a Scheme of Arrangement or Reduction of Capital process.** Actual redemption of preference shares will not need this. However, the conversion of equity shares to redeemable preference shares will need to be done only through Scheme of Arrangement and NCLT approval.

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Online Gaming or Gambling?

Background:

Gaming is one of the most immersive forms of entertainment. The Indian gaming Industry has seen a significant growth in last couple of years (thanks to restriction on movement of people during lockdown). India is home to one-tenth of the world's gamers and the number of game-development companies here has gone from just 25 in 2010 to 250 in 2019.Further It has seen a rapid growth owing to investment from biggies like Nazara, Tencent, Azure among several others.

According to the report released by KPMG in 2022, India's online gaming market had revenue of INR 136 billion ($1.80 billion) and is predicted to expand at a CAGR of 21% over the next five years leading up to INR 290 billion ($3.84 billion). The industry estimates that it has the potential to attract FDI of more than INR 10,000 crore over the next few years.

Is it regulated?

At present online gaming does not have independent legal recognition, having to shelter under an undefined exception to the state gambling and public order laws and as every state has their own regulations to address the harms posed by the gaming sector leading to categorising same as legal in one and illegal in another state.

There is a very thin line of difference between gaming and gambling. The main difference between the terms gaming and gambling is that for gaming the outcome is achieved by skill, not chance and it is opposite in case of gambling. The same is recognised in various High Court Judgements and some Supreme court judgements.

Present scenario

Presently every state has their own regulations and therefore whether it will be treated as game of chance or skill, there is no harmony in it which leads to an ambiguous situation. Therefore, in order to recognise online gaming as a game of skill and to promote growth and innovation of this industry while securing consumer interest, NITI Aayog submitted some recommendations.

Considering the suggestions, Centre appointed the Ministry of Electronics and Information Technology (MeitY) as the nodal ministry for matters relating to online gaming with monetary risks and proposed amendments in The Information Technology (Intermediary Guidelines and Digital Media Ethics Code) Rules, 2021 which were available for public comments in January, 2023.

The draft amendment proposed by the MeitY direct online games to be registered with the self-regulatory bodies (SRB) registered with the ministry. SRB shall provide registration if the game does not "contain anything which is against the interest of sovereignty and integrity of India, defence of India, security of the State, friendly relations with foreign States or public order" and is in conformity with other laws, including laws related to gambling and betting.

Foreign Investment in Online Gaming Industry?

FDI in India is regulated by Foreign Exchange Management (Non-Debt Instruments) Rules, 2019 [NDI Rules]. Gambling and betting including casinos are included in the list of prohibited sectors for FDI under the NDI Rules. Further there is no specific sector included in NDI rules to include online gaming Industry.

As the Gambling and betting is clearly recognised as prohibited sector, the important factor will be to prove how it is in conformity with the applicable laws related to gambling and betting and why the same should not be considered as gambling.

Whether it is allowed to accept foreign investment and under which sector and any other conditions required to be fulfilled for the same? The same shall be discussed in our next article. Stay tuned.

Rules: - In conflict with the Act or a pillar to count on Applicability of CSR

Section 135(1) of the Companies Act (the Act) states that **Every company** having net worth of rupees 500 crore or more, or turnover of rupees 1,000 crore or more or a net profit of rupees 5 crore or more during the immediately preceding financial year shall constitute a Corporate Social Responsibility (CSR) Committee of the Board consisting of three or more Directors, out of which at least one director shall be an independent director.

If we apply Rule of Literal Interpretation and interpret the word **'Company'** as per Section 2(20) of the Act, it means a company incorporated under this Act or under any previous company law.

However, if we read Section 135(1) alongwith Rule 3(1) of Companies (Corporate Social Responsibility Policy) Rules, 2014 (CSR Rules), it states that a **'Company'** means **Every company including** its holding or subsidiary, and a **foreign company** defined under clause (42) of section 2 of the Act having its branch office or project office in India, which fulfils the criteria specified in sub-section (1) of section 135 of the Act, shall comply with the provisions of section 135 of the Act and these rules.

Rules in conflict with the Act?

Section 469 of the Act empowers Central Govt. to make rules and CSR rules are prescribed according to it. Further, two conditions must be fulfilled before a rule can have the effect of a statutory provision (1) it must conform to the provisions of the statute under which it is framed; and (2) it must also come within the scope and purview of the rule making power of the authority framing the rule. If either of these two conditions is not fulfilled, the rule so framed would be void.

Further as per rules of interpretation, the basic principle that the legislature delegates because it cannot directly exert it's will in every detail. All it can in practice do is to lay down the outline. This means that the intention of the legislature, as indicated in the outline (that is the enabling Act), must be the prime guide to the meaning of delegated legislation and the extent of the power to make it. Its primary use is to supplement Acts of Parliament by prescribing the detailed and technical rules required for their operation.

In the case of Companies Act, 2013, Section 469 of the Act empowers Central Govt. to make rules and CSR rules are prescribed according to it. Further if we read Section 135(1) alongwith Rule 3(1) of CSR Policy rules, 2014 prima facie it appears that as the word "Every Company" is used and therefore it will be applicable to companies incorporated in India under provisions of the Act or previous law as stated earlier also, but then rule 3(1) elaborates it further and includes every Company, its holding or subsidiary, and a foreign company defined under clause (42) of section 2, prima facie it appears that the rule is going beyond what the Act contemplates and expanding the meaning of Company.

Whether Rule 3(1) of the CSR Rules is in consonance with Section 135(1) of the Act?

Usually, every statute has a definition section and it is a sound rule of construction to give the same meaning to the same words occurring in different parts of an Act of Parliament. But generally, definitions clause of every Act starts with the words unless the context otherwise requires. Therefore, a term defined in the definition section will hold unless the context requires otherwise. Even where the definition is exhaustive inasmuch as the word defined is said to mean a certain thing, it is possible for the word to have a somewhat different meaning in different sections of the Act depending upon the subject or the context. Therefore, while interpreting the word has to be read in the light of context and the object for which the act was made by the legislature.

If we read Section 135(1) along with Rule 3(1) by applying above rule of interpretation, it appears that intent of legislature was not to restrict the CSR obligations to Companies incorporated under the Act or previous law, to supplement this intention the rule 3(1) was prescribes which elaborates the meaning of word Company and therefore it includes a foreign company as defined in Section 2(42) having a branch or project office of a foreign company.

Therefore, if we resort to interpretation principle of purposive interpretation, it seems to appear that Rule 3(1) of the CSR Rules is in consonance with Section 135(1) of the Act.

Filing of Certain forms in physical mode with the concerned Registrar.

The Ministry of Corporate Affairs has rolled out 45 new web based forms from 23rd January, 2023. In a process of stabilizing the transition of MCA portal, MCA has permitted to file certain e-forms in physical mode with concerned Registrars of Companies pursuant to representation made by its stakeholders as these forms are required to be filed due to time bound activities.

Companies intending to file following forms from 22nd February, 2023 to 31st March, 2023 may file such forms in physical mode duly signed by the persons concerned as per requirements of the relevant forms along with a copy thereof in electronic media, with the concerned Registrar without payment of fee and take acknowledgement.

1. GNL-2 (filing of prospectus related documents and private placement)
2. MGT-14 (Filing of resolutions relating to prospectus related documents and private placement)
3. PAS-3 (Allotment of Shares)
4. SH-8 (Letter of offer for buyback of own shares or other securities)
5. SH-9 (Declaration of Insolvency)
6. SH-11 (Return in respect of buy-back of securities)

Such physical filing will be accompanied by an Undertaking from the company that, the Company shall file the relevant form in electronic mode on V3 MCA-21 Portal along with fees payable.

Circular can be accessed on following link: https://www.mca.gov.in/bin/dms/getdocument?mds=L1%252FlzzFGRvjYOFmh0PQHAw%253D%253D&type=open

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SEBI Consultation Paper on Streamlining Disclosures By Listed Entities And Strengthening Compliance With SEBI LODR Regulations

Securities and Exchange Board of India ("SEBI") has issued a **Consultation paper** on **February 20, 2023** on proposed amendments to SEBI (Listing Obligations And Disclosure Requirements) Regulations, 2015 [‘LODR Regulations"] on below aspects:-

- Streamlining Disclosures by Listed Entities, and
- Strengthening Compliance with LODR Regulations

The timeline for submission of comments on this Consultation paper to SEBI is March 6, 2023. The highlights of proposed amendments in this Consultation paper are as follows:-

Sl. no	Reg no.	Nature of amendment	Proposed Amendment
1	Regulation 33 – Financial Results	Insertion	**Submission of first financial results by newly listed entities:** Currently timelines prescribed under Reg. 33 of LODR Regulations for submission of quarterly financial results, i.e., 45 days from end of first three quarter of financial year and 60 days from end of last quarter, are applicable to first time listed entities also. SEBI has received representation highlighting difficulties faced by these companies in submitting quarterly results and financial statements, specially by entities which get listed towards the end of 45 days period as they get very less time after listing to prepare financial results. Hence in order to provide reasonable timeline for such entities, following points are proposed for discussion by SEBI:- • For entities which get **listed during the first 45 days of a quarter**, it is proposed to provide a minimum time period of 15 days for newly-listed entities for disclosure of first financial results (of the preceding quarter) post their listing on stock exchanges. • Further if any entity gets **listed on stock exchange during the latter part of 45 days in a quarter** (or during the last 30 days in case of listing during first quarter of financial year), even then the financial results for the quarter(s) preceding date of listing (all quarters succeeding the disclosure made in offer documents for initial public offer) also needs to be filed

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with stock exchanges, within 15 days of listing. As of now, there is no requirement to file financial results of those preceding quarter(s), as the entity would have got listed post the end of timeline prescribed under Regulation 33 for submission of previous quarter's financial results.
For eg: if a company gets listed on Feb 15 or post that till March 31, then in that case it is proposed to mandate such listed company to disclose results for December quarter within 15 days of listing. It means that if a company gets listed on Feb 15 then it will have to disclose financial results for quarter ended 31 December by March 2, and if it gets listed on March 31 then it will have to disclose financial results for quarter ended 31 December by April 15.
<table>
<tr><td>Listing date</td><td>Current requirement</td><td>Gap</td><td>Proposed for dec quarter results (for eg.)</td><td>Gap between listing and disclosure date</td></tr>
<tr><td>Jan 01</td><td>By Feb 14</td><td>44 days</td><td>By Feb 14</td><td>44 days</td></tr>
<tr><td>Jan 15</td><td>By Feb 14</td><td>30 days</td><td>By Feb 14</td><td>30 days</td></tr>
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<tr><td>Feb 15</td><td>NA</td><td>NA</td><td>By March 1</td><td>15 days</td></tr>
<tr><td>March 31</td><td>NA</td><td>NA</td><td>My April 15</td><td>15 days</td></tr>
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<tr><td>2</td><td>Regulation 17(1) and 25(6) – Filling of</td><td>Insertion</td><td>Timeline to fill up vacancy of directors, Compliance Officer, Chief Executive Officer (CEO) and Chief Financial Officer (CFO) in listed entities:</td></tr>
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Sl. no	Reg no.	Nature of amendment	Proposed Amendment
	vacancy of Key Management Personnel		**Filing of vacancy of director - Insertion in Regulation 17(1) and deletion of Regulation 25(6):** It proposed that any vacancy arises in the position of any director, which results in non-compliance happens with regard to composition of board as compared to the composition prescribed in Regulation 17(1), either due to cessation of any director (independent directors or any other director) due to resignation, removal, death, disqualification or completion of tenure OR due to appointment of any non-independent director OR due to change in designation of an existing director, then such vacancy shall be filled up within a period of three months from the date vacancy. Since this proposed regulation will cover all possible scenarios of vacancy of director, SEBI is also proposing to remove specific requirement of filling of vacancy in the position of independent director arising out of resignation and removal under Reg 25(6) as it only envisages two scenarios. Viz. removal and resignation of independent director only. **Filing of vacancy of Compliance officer, CEO and CFO (Collectively as 'KMPs') –** Considering the gravity of the responsibilities entrusted on the compliance officer, CEO and CFO of a listed entity, there felt a need to specify a reasonable timeline within which a vacancy arising for such officers should be filled up by the listed entity. In this regard SEBI is proposing that any intermittent vacancy in the position of Compliance Officer, CEO and CFO shall be filed up by listed at the earlies but not later than a period of three months. This is in deviation to OR stricter than the timeline of six months as provided under Companies Act, 2013 for filing up the vacancies of KMPs.
3	Regulation 98(1) - Liability for contravention of the Act, rules or the regulations.		**Freezing of demat accounts of the Managing Director(s), Whole-time director(s) and CEO(s) of a listed entity for continuing non-compliance with the LODR Regulations and / or non-payment of fines by a listed entity:** Penal provisions as mentioned in Regulation 98 of LODR work well for promoter-driven companies, the same may not be relevant for companies without any identifiable promoters. It is observed that increasing number of professionally managed companies (without any

Sl. no	Reg no.	Nature of amendment	Proposed Amendment
			identifiable promoters) are getting listed on the Stock Exchange(s) and they are out of purview of freezing provisions in case they are continuously in non-compliance of provisions of LODR Regulations and / or non-payment of fines levied on the entity. Hence, it is proposed that the **demat account of the WTDs, including the MD, and CEO(s) may be frozen,** in addition to the demat account(s) of the promoters, for continuing non-compliance and / or non-payment of fines by a listed entity. SEBI has also proposed that the demat accounts MD(s) / WTD(s) / CEO(s) who resign from a non-compliant entity shall be unfrozen after the listed entity complies with the applicable provisions of the LODR Regulations and / or pays the outstanding fines, or on the 90th day from the date of getting relieved from the company, whichever is earlier. The new MD / WTD / CEO shall be given 90 days' time from the date of assuming charge to ensure the listed entity's compliance with the applicable provisions and payment of outstanding fines, failing which their demat account(s) shall be frozen. The same shall be incorporated in the SoP circular.

The link for this Consultation Paper is given below:-

https://www.sebi.gov.in/reports-and-statistics/reports/feb-2023/consultation-paper-on-streamlining-disclosures-by-listed-entities-and-strengthening-compliance-with-sebi-listing-obligations-and-disclosure-requirements-regulations-2015_68194.html

SEBI reviews provisions relating to Buyback and makes it Investor friendly

Securities and Exchange Board of India ('SEBI') vide its notification dt: February 7, 2023 has brought in SEBI (Buyback of Securities) (Amendment) Regulations, 2023. **This is effective from the thirtieth day of notification of the amendment in the official gazette i.e. effective of the amendment is March 9, 2023.** A detailed analysis of this amendment is given below:-

A. Changes in universally applicable provisions of buyback

a. **Calculating the quantum of buyback:**

i. **Existing provision:** Reg. 4(i) of SEBI (Buyback of Securities) Regulations, 2018 [Buyback Regulations'] provides for the maximum quantum of Buyback. Before amendment, it stated that the maximum limit of any buy-back shall be twenty-five percent or less of the aggregate of paid-up capital and free reserves of the company, based on both standalone and consolidated financial statements of the company.

ii. **Background of Amendment:** As is stated above, prior to the amendment as per Reg. 4(i) of Buyback Regulations, maximum quantum of buyback was required to be calculated based on consolidated and standalone financial statements of the listed company. This was creating confusion as to whether consolidated or standalone financial statements shall be used?

iii. **Amendment:** In order to clear this confusion, SEBI has now amended Reg. 4(i) of the Buyback Regulation which now states that the maximum quantum of buyback will be required to be calculated on the basis of consolidated or standalone financial statements of the listed company, **whichever sets the lower amount**. Throughout the Buyback Regulations, wherever the wording was 'standalone **and** consolidated financial statements', these wordings are now replaced with 'standalone **or** consolidated financial statements'. This has put to rest confusion relating to the calculation of the quantum of buyback under any method of buyback.

b. Methods of buyback:

i. **Introduction:** SEBI had received many representations with respect to reviewing the methods of buyback. Further SEBI had also witnessed that there was a need to review existing modes of buyback due to many representations of change in perspective and practical difficulties. SEBI found that method of buyback relating to *'odd lots'* is not relevant as of now as trading lot in market is of one share. With this intent a need was felt to review the methods of buyback.

ii. **Background of Amendment: As per Regulation 4(iv) of Buyback Regulations,** A company may buy back its shares or other specified securities by any one of the following methods:
   1. from the existing shareholders or other specified securities holders on a proportionate basis through the tender offer;
   2. from the open market through stock exchange;
   3. from odd-lot holders:

iii. **Amendment:** After deliberations at the board meeting on the recommendations of sub-group it was decided to withdraw the method of **buyback through the odd lot** and all related provisions relating to that are also withdrawn by SEBI.

c. **Consent Requirements:** It was suggested that for the sake of transparency, consent of lenders should be made necessary for buyback in case there is a breach of any covenant with such lender(s). If consents are required from the company's lenders, a disclosure should be included in the public announcement, the explanatory statement circulated to the company's shareholders and/or a letter of offer to this effect. The sub-group proposed and SEBI accepted that Schedules I (Contents of explanatory statement) and Schedule IV (Public Announcement for Open Market Buy Back through Stock Exchange) of Buyback Regulations should be amended to include such obligation.

d. **Dispensing with the need of submitting physical documents and instead permitting submission of soft copies to SEBI:** To promote ease of doing business and leverage the advancement in technology, it is proposed that the companies shall submit to SEBI, all the relevant documents as specified in the Regulations, electronically and digitally signed by the company secretary of the company or the person authorized by the board of directors of the company, undertaking buy-back.

e. **Post-buyback compliance:** Companies will undertake the extinguishment and physical destruction of share certificates in the presence of the secretarial auditor as they conduct the secretarial audit of the company and ensure better compliance in terms of SEBI regulations and other allied laws. Before amendment, this was to be done in the presence of statutory auditor.

f. **SEBI has now harmonized the timing of payment of fees.** It is **to be paid SEBI on the date of public announcement across all available routes** under buy-back.
Earlier in case of open market buyback, fees was to be paid at the time of filing copy of the public announcement, whereas in case of buy back through book building process, it was to be paid within 2 days of public announcement, whereas in case of buyback through tender offer route, it was to be paid along with draft letter of offer.

g. **The time limit for filing a copy of the resolution with SEBI and Exchanges:** Seven working days provided now as against seven days earlier for filing a copy of the resolution passed at the general meeting under section 68(2) of the Companies Act, 2013 with SEBI and Stock exchanges.

SEBI has accepted the terminology of 'working days' in buyback regulations as against 'days' used earlier. So listed entities would effectively get more time for compliance or disclosure-related provisions.

h. **Duration of tendering period:**

   i. **Existing regulation:** Regulation 4(vi) of Buy Back Regulations states that the offer for buy-back shall remain open for a period of ten working days.

   ii. **Background of Amendment:** In terms of SEBI (Delisting of Equity Shares) Regulations, 2021, the duration of the tendering period in case of voluntary delisting offers is five working days. Accordingly, a need was felt to harmonize the duration of the tendering period under buy-backs in line with the delisting offers and reduce the duration of the tendering period from ten working days to five working days.

   iii. **Amendment:** The offer for buy-back shall remain open for a period of five working days. For open market buyback SEBI has separately prescribed tendering period depending on time limits for phasing out of buybacks (which is explained in below part of this article).

i. Payment of consideration to shareholders:

   i. **Existing Provision:** Regulation 10(ii) of Buy Back Regulations, inter-alia, requires company to make payment of consideration to those holders of securities whose offer has been accepted within seven working days of the closure of the offer.

   ii. **Background of Amendment:** SEBI, vide circular dated August 13, 2021, has streamlined the process of tendering of shares in open offers, buy-back offer and delisting offer and the shares tendered by the shareholders are now being blocked in the demat account of the shareholders as against the earlier practice of transferring physical shares to the clearing corporation, which ensures the transfer of funds/securities happens in a secure, seamless and prompt manner. Further, the period for payment of consideration in the delisting offers is already five working days.

   iii. **Amendment:** It was approved that the payment of consideration shall be completed within five working days after the closure of the tendering period.

j. Taxation matter:

   i. **Existing provision:** With effect from July 05, 2019, the provisions of section 115QA of the Income Tax Act, 1961 were amended to levy buyback tax on the income distributed by the listed company through buyback of equity shares of the said listed company, thus changing the incidence of tax from the hands of shareholders (who offer their shares under the buy back) to that of the listed company. In subsequent amendment to the Finance Act, 2020, dividend distribution tax was abolished, thereby shifting the incidence of tax on dividends in the hands of recipients at the applicable rates.

   ii. **Background of Amendment:** The current mechanism of buyback tax appears to be tilted in favour of those shareholders who tender their shares and take exit (partially or fully) from the company and adversely impacts the interest of shareholders who do not wish to tender their shares under buyback. As a result, all the continuing shareholders have to share the burden of tax payable by the listed company on the buyback proceeds of the shares tendered by exiting/tendering shareholders. In other words, the tax under section 115QA has to be paid by the company from its free reserves on behalf of the exiting shareholders and promoters at the cost of continuing shareholders.

iii. **Proposal:** SEBI has in its SEBI Board Note pertaining to discussion on amendment to SEBI (Buyback of Securities) Regulations, 2018 during SEBI board meeting held on December 20, 2022 has mentioned that it has proposed to the Government of India to shift the incidence of tax on buyback from company to the hands of shareholders tendering their shares in buy back.

k. **Filing of public announcement with SEBI and stock exchanges:** Listed entity shall, simultaneously with publishing the public announcement as per Regulation 7(i) of SEBI (Buyback of Securities) Regulations, 2018 [i.e. publishing of public announcement in newspapers] file a copy of the public announcement in electronic mode, with SEBI and the stock exchanges on which its shares or other specified securities are listed**.** Earlier this clause mentioned about filing with SEBI only and mode of filing was in physical mode only.

l. **Escrow Account:** The company shall be required to open an escrow account, within two working days of the public announcement.

i. **Background:** Currently, the Buy-Back Regulations require the company to open an escrow account towards security for performance of its obligations under the regulations, before the opening of the offer. Further, the escrow account may be in form of cash deposited with any scheduled commercial bank or a bank guarantee issued by any scheduled commercial bank in case of buy-back through open market. Along with the these, an additional means of depositing acceptable securities (with appropriate margin) is also permitted in case of buy-back through tender offer.

ii. **Anomaly:** Buy-Back Regulations did not specify an exact date of opening of an escrow account as provided under other regulations, viz. SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 and SEBI (Delisting of Equity Shares) Regulations, 2021. Further, a need was felt to align the different modes of deposit in the escrow account prescribed across all the routes of buy-back.

iii. **Amendment:** With regard to concern expressed regarding administrative difficulties that may be faced by the listed companies, it is stated that under the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 and the SEBI (Delisting of Equity Shares) Regulations, 2021, an escrow account is already mandated to be opened within two working days from the date of public announcement and thus, there seems to be no reason for a listed entity for not adhering to the same, in case of buyback offers.

Additionally, to ensure smooth compliance and give more options to the Company, certain additional modes have been added to fund the escrow account for the purpose of the buyback. The securities mentioned shall be subject to the appropriate margin as specified by SEBI.

A Comparison of permissible items in escrow account pre and post amendment is as follows:-

Pre Amendment – Escrow A/c	Post Amendment – Escrow A/c
Cash deposited with a scheduled commercial bank	Cash **including bank deposits** deposited with any scheduled commercial bank
Bank guarantee in favour of the merchant banker	Bank guarantee issued in favour of the merchant banker **by any scheduled commercial bank**
Deposit of acceptable securities with appropriate margin.	Deposit of **frequently traded and freely transferable equity shares or other freely transferable securities**
	Government securities
	Units of mutual funds invested in gilt funds and overnight schemes
Combination of above	

Further with a view to Rationalizing certain requirements in case of an escrow account across all routes of Buy-back, it is stated by SEBI that - Where part of an escrow account is in the form other than cash (earlier it was applicable if escrow account was in form of bank guarantee), there will be requirement of depositing cash of at least 2.5% of the total amount earmarked for buy-back uniform across all applicable routes of buy-back, viz: through open market and through the tender offer.
Further earlier the validity of bank guarantee could be till all the obligations are completed or 30 days from expiry of buy-back period, whichever is later. This timeline has been **changed from 30 days to 30 working days**.

B. Buyback through tender offer route:

a. **Total Limit for Buy-backs:** Section 68(2)(c) of the Companies Act, 2013 provides that a company can buy-back its shares up to twenty-five per cent or less of the aggregate of paid-up capital and free reserves of the company. In similar lines, regulation 4(i) of the Buyback Regulations, 2018 provides that the maximum limit of any buy-back through tender offer route shall be twenty-five cent or less of the aggregate of paid-up capital and free reserves of the company, based on both standalone and consolidated financial statements of the company. It was suggested that since buy-backs through tender offers are an efficient way of returning surplus funds to the shareholders, the maximum limit may be enhanced.

   Proposal: Accordingly, the sub-group recommended that for buy-backs undertaken through tender offers, the limit of buybacks in any financial year can be enhanced to 40% of the aggregate paid-up capital and free reserves of the company based on the standalone or consolidated financial statements of the company, whichever sets out a lower amount. This would help companies return surplus cash to shareholders. Also it was stated that this would be applicable to companies who are net debt free. This discussion forms part of SEBI board meeting note pertaining to discussion on amendment to SEBI (Buyback of Securities) Regulations, 2018.

b. Cooling-off Period between Buy-backs

i. **Introduction:** Some companies, who may need to return surplus cash to their shareholders more than once within a period of one year reckoned from the date of expiry of buy-back period of the preceding offer of buy-back which should be facilitated under the regulations.

ii. **Background:** Proviso to section 68(2)(g) of the Companies Act, 2013 mentions that no offer of buy-back shall be made within a period of one year reckoned from the date of the closure of the preceding offer of buy-back, if any.

Accordingly, regulation 4(vii) of the Buyback Regulations, 2018 also restricts company from undertaking any offer of buy-back within a period of one year reckoned from the date of expiry of buy-back period of the preceding offer of buy-back, if any.

iii. **Proposal:** Companies should be allowed to undertake up to two buy-backs within a period of one financial year provided that such buy-backs are undertaken through the tender offer route only and such buy-backs shall be subject to the annual limit of 40% of the paid-up capital and free reserves of the company. This discussion forms part of SEBI board meeting note pertaining to discussion on amendment to SEBI (Buyback of Securities) Regulations, 2018.

As we have seen above SEBI has already notified date for making effective amendments to provisions of Buyback Regulations. But the challenge here is that provisions of Companies Act, 2013 are not in sync with the revised buyback regulations. Accordingly, SEBI has made representation to Ministry of Corporate Affairs to review the provisions of buyback in the context of amendment made by SEBI to buyback regulations.

c. Change in buyback price:

i. **Background for Amendment:** As per the timelines prescribed for various activities under the extant Buy-back Regulations, there is a substantial delay between the time when the buy-back is approved by the board or shareholders, as may be applicable, and the time when the buy-back offer is actually opened but despite such time gap, the buy-back price remains the same as was approved by the board or shareholders and there is no provision for allowing the company to revise the offer price subsequently.

ii. **Amendment:** It was deliberated that any increase in buy-back price will cause corresponding reduction in number of shares to be bought back, thus leading to change in the entitlement ratio of the shareholders, and if the offer price is allowed to be changed just prior to opening of the buy-back offer, it may cause uncertainty amongst the shareholders. In order to neutralise this possibility, the suggestion of the commenters to link the upward revision of price with the record date (not prior to opening of offer), SEBI has inserted Regulation 5(via) to the effect that in case of a buy-back through tender offer, the Board of Directors of the company may, till one working day prior to the record date, increase the maximum buy-back price and decrease the number of securities proposed to be bought back, such that there is no change in the aggregate size of the buy-back.

d. Review of Draft Letter of Offer & giving comments by SEBI:

i. **Existing Provision:** Regulation 8(1)(a) requires the company, through a merchant banker, to file a draft letter of offer ("DLOF") with SEBI and subsequently, SEBI has provided a window of seven working days (extendable to the seventh working day from the date of satisfactory reply to the clarification or additional information sought) to submit its comments on the same.

ii. **Issues:** A need was felt to simplify the process and to reduce the timelines so as to ensure that buy-back offer starts promptly. Further it was seen that there is no requirement of review of letter of offer by SEBI in case of buy-back from open market.

iii. **Amendment:** In this regard in case of the buy-back from **open market (stock exchange route), the requirement for submission of draft letter of offer with SEBI for its comments has now been deleted**

C. Open market buybacks:

Why review of open market buyback provisions?
SEBI has adjudicated in few cases whereby it was seen that company had not placed buyback offers for a period of around five months from commencement of tendering period of buyback and all orders for buying shares from open market buyback were placed in the last month. This not only resulted in disruption in market price but also company found it difficult to fulfil the buyback commitment. These cases might also be one of the reasons why SEBI is considering review of open market backs. Hence it was deliberated whether to retain this mode of buy back at all?

a. Phasing out of open market buybacks:

i. **Existing Provision:** Proviso to Regulation 4(iv) of Buy Back Regulations provides that the buy-back size from open market through stock exchange shall be less than fifteen per-cent of the paid-up capital and free reserves of the company, based on both standalone and consolidated financial statements of the company. Further, Regulation 17(ii) of these Regulations provides a time period of six months from the date of opening of the offer, for the buy-back offer to be closed.

ii. **Background for Amendment:** Under the stock exchange route, there is a possibility of the entire sell order of any shareholder of the relevant listed entity, getting matched with the purchase order placed by the company, irrespective of the fact if the said selling shareholder intended to offer his/her shares to the said company pursuing its buy-back on the exchange. Further, one such shareholder's entire sell order getting matched with the purchase order placed by the company tantamount to depriving other shareholders, who want to avail the benefit of buy-back including the tax benefit embedded therein, which runs contrary to the underlying principle of equitable treatment of all shareholders that forms the bedrock of all the corporate actions. Further, an extended period of six-months' time permitted to the listed entities for keeping the buy-back offer open through the stock exchange route, may result in artificial demand being created on the exchange platform for the relevant company's shares for a long period of time, thereby, preventing efficient price discovery of that scrip. Deliberations were done with respect to enhancing the utility of buyback for shareholders and simultaneously phasing out open market buyback method was recommended by Primary Markets Advisory Committee. It was also discussed that acceptance of shares from the shareholders offering their shares under buy-back through tender offer route is more equitable (than the stock exchange route) as the shares are accepted from the shareholders in a proportionate manner as against stock exchange route, where acceptance of shares offered under the buy-back offer of a company, is more of a matter of chance due to price-time order matching mechanism of the stock exchange platform. Further, it is also worth stating that, the companies generally buy-back shares at a price, which seems advantageous to the company rather than offer a price which shall be beneficial to its shareholders. Further from tax angle it was noted that under the buy-back exercise through the stock exchange route, while some shareholders will be able to offload their entire shareholding because of their sell orders entirely matching with the buy orders placed by the listed entity and will not have to pay any tax on their gains, other shareholders who also want to offer their shares to the said company but their offers could not match with the purchase orders placed by the company under its buy-back offer, remain deprived of the benefits expected by them from the said buy-back offer of the company thereby rendering the stock exchange route iniquitous. Considering the above it was recommended to phase out open market buybacks.

iii. **Amendment:** In this regard SEBI has approved systematic phasing out of open market buybacks. Open market buybacks will be completely phased out from April 1, 2025. Till then open market through stock exchanges, based on the standalone or consolidated financial statements of the company, whichever sets out a lower amount, shall be less than:—
   i. fifteen percent of the paid-up capital and free reserves of the company till March 31, 2023;
   ii. ten percent of the paid-up capital and free reserves of the company till March 31, 2024;
   iii. five percent of the paid-up capital and free reserves of the company till March 31, 2025

b. Minimum utilization of the amount earmarked for buy-back:

i. **Existing Provision**: Regulation 15 of Buy Back Regulations requires companies to ensure that at least 50% of the amount earmarked for a buy-back through stock exchange route, as specified in the resolution of the board of directors or shareholders, is utilized. However, relaxation in respect of such a requirement prescribed under Regulation 20(viii) of these Regulations is granted in certain situations which are specified below:

- If the volume weighted average market price of the specified securities of the company during the buy-back period was higher than the buyback price;
- If sell orders from shareholders were inadequate despite the buy orders placed by the company; or

- If there existed such circumstances which were beyond the control of the company and in the opinion of the SEBI merit consideration.

ii. **Background for Amendment:** It has been observed in the past that companies, after announcing their buy-back offer through the stock exchange route, tend to purchase shares towards the close of the buy-back period which sometime results in artificial impact on the price discovery of the scrip. Therefore, in order to arrest such a practice and to ensure that shares are bought back on a consistent basis in a staggered manner over the course of the buy-back period without affecting the price discovery mechanism on the stock exchange platform, a proposal was made to mandate utilization of at least 40% of the amount earmarked for buy-back within half of the duration of the buyback period as specified under the proposed glide path which appeared to be reasonable and logical. Further, it is reiterated that buy-back through this route is proposed to be made applicable only for frequently traded scrips (as explained in below paras) and thus, the concerns expressed with respect to constraints that may be faced by the companies having low trading volume to comply with the above proposal are misplaced on facts hence, irrelevant.

iii. **Amendment:** SEBI has now prescribed that at least 40% of the amount earmarked for buyback be utilized within the initial half of the financial year. Also, it has stated that min. 75% of the amount earmarked for open market buyback shall be utilized as against 50% earlier.

c. Separate Window for buybacks:

i. **Existing Provision:** Currently, a listed company undertakes buy-back through stock exchange route by purchasing from sellers on the stock exchange(s) having nationwide trading terminals through an order matching mechanism.

ii. **Background for Amendment:** Since shares are bought back at the prevailing market prices, acceptance of shares under buy-back is a matter of chance for most of the shareholders. This is because the trading platform of stock exchange offers no clarity as to whether shares sold by the shareholders on the stock exchange platform have been accepted under a buy-back offer or they were sold in open market as a regular trade and in the process. Hence the shareholders are unable to avail the benefits arising out of buy-backs.

iii. **Amendment:** Open market buybacks whose issue opens after the date of this amendment will be executed through a separate window on stock exchange and not under order matching mechanism.

d. Reduction in timeline for tendering shares in open market buyback:
SEBI has also curtailed timelines for a period of tendering for open market buybacks: The buy-back offer shall open not later than four working days from the record date and shall close:-

i. within six months, if the buy-back offer is opened on or before March 31, 2023;

ii. within 66 working days, if the buy-back offer is opened on or after April 1, 2023, and till March 31, 2024; and
iii. within 22 working days, if the buy-back offer is opened on or after April 1, 2024, and till March 31, 2025:

Provided that with effect from April 1, 2025, the option of open market buy-back through the stock exchange shall not be available to any company except in cases where the buyback offer has opened on or before Mach 31, 2025.

e. Open market buyback only for frequently traded shares:

i. **Existing Provision:** Currently, there is no eligibility requirement specified for open market buy back and all the listed companies can undertake buy-back through this route.

ii. **Background for Amendment:** It is observed that the buy-backs through stock exchanges are efficient in cases where the shares of the relevant company are frequently traded. In such cases, the trading price is reflective, by and large, of the market value of the company's shares, which is not the same in respect of listed companies whose shares are not frequently traded. Further, it may also be noted that it will not be possible to implement the pricing restrictions, in case of the companies whose shares are not frequently traded.

iii. **Amendment:** In this regard it was stated that while buy-back provides an opportunity to the shareholders of infrequently traded scrip to exit from the company, however, it will be erroneous to suggest that the objective of buy back through stock exchange route should be to impart liquidity to an infrequently traded scrip. Therefore, it is all the more important that each shareholder is given an equal opportunity to tender their shares, which is possible if the company undertakes buy-back through tender offer route rather than stock exchange route. Hence it was decided to allow Buyback through the stock exchange only to companies whose shares are frequently traded. Also, SEBI has introduced the definition of frequently traded shares in Buy Back Regulations. The definition is same as that is provided under SEBI (Substantial Acquisition of Shares and Takeover) Regulations, 2011.

f. Restrictions on Volume and Price:

i. Currently, there are no pricing-related restrictions specified under the Buy-back Regulations in respect of buy-backs undertaken through the stock exchanges.

ii. **Background for Amendment**: SEBI was concerned with price manipulation pursuant to open market buybacks. It was discussed at SEBI board meeting that absence of any restrictions on trading volumes with respect to open market buyback may result in situations where the trading price of the company's shares is exaggerated due to ongoing buy-back of shares by a company. Restricting pricing and volumes of buying shares in open market buyback by listed entity is necessary to prevent any intervention in the price discovery or disruption in the market integrity of the scrip that may be caused due to buy back orders being placed on the stock exchange platform. Further discussion were done on various technical aspects pertaining to placing of orders during open market buybacks.

iii. **Amendment:** On deliberations as discussed above it is decided that on any particular trading day,. the company shall not purchase more than 25% of the average daily trading volume (in value) of its shares or other specified securities in the ten trading days preceding the day in which such purchases are made. The company shall not place bids in the pre-open market, first thirty minutes and the last thirty minutes of the regular trading session. The company's purchase order price should be within the range of (+/-) 1% from the last traded price

D. Buyback through Book building:

The revised mechanism for open market buybacks through the book building process is notified**.** In this regard, SEBI noted that companies have not preferred the book building route for undertaking buy-backs, and except for one company (in the year 1998), no other company has undertaken buy-back through this route to date. However, in view of the recommendations of PMAC and the comments received, it is proposed to introduce the revised framework, initially for one year from the date of notifications, after which the framework shall be reviewed. The summary of proposals is provided below-

I. Announcement - The public announcement relating to the buy-back will be published within two working days of the date of board or shareholders' approval, as the case may be.

II. Opening of the Offer- The book-building process will commence within seven working days from the date of public announcement.

III. Buy-back Price: In the public announcement, the company will disclose:
   a. maximum buy-back price approved by the company's board of directors or shareholders; and
   b. book value of the company's securities.

   Further, in the offer opening announcement, a price range will be disclosed.

IV. Retail Participation- Retail investors will have the option to bid at the cut-off price.

V. Promoter participation- Promoters along with their associates will not be permitted to participate in such a method of buy-back.

VI. Payment- The payment of consideration to shareholders will need to be completed within a period of five working days following the closure of the buy-back offer.

VII. Withdrawal- Once the public announcement is made, the buy-back cannot be withdrawn or terminated.

VIII. Acceptance Methodology
   1. The buy-back offer will be kept open for a minimum of two trading days.
   2. Shareholders can submit bids for any number of shares (not exceeding the total number of shares in the relevant category) at a price within the price range.
   3. If the bids are more than the buy-back size:
      - The price at which 100% of the buy-back size is reached will be the clearing price; and

- Shares tendered at or below the clearing price will be accepted at the clearing price (and in proportion to the size of the bids received).

4. If the bids are less than the buy-back size, all the shares tendered will be accepted at the highest bid price.
5. Bids once placed cannot be withdrawn.

E. Conclusion:

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With this amendment, lot of changes have been brought into the framework for undertaking buy backs by listed companies. This will go a long way in reducing market manipulations incidental to buy back and will also help in making the Buy Back process much more investor friendly.

MMJC

SEBI Consultation Paper on Strengthening Corporate Governance of Listed Entities by Empowering Shareholders through LODR Regulations

Securities and Exchange Board of India ("SEBI") has issued a **Consultation paper** on **February 21, 2023** on proposed amendments to SEBI (Listing Obligations And Disclosure Requirements) Regulations, 2015 [`LODR Regulations"] on below aspects:-

- Agreements binding listed entities
- Special rights granted to certain shareholders
- Sale, disposal or lease of assets of a listed entity outside the 'Scheme of Arrangement' framework and
- 'Board Permanency' at listed entities / Need for periodic review.

The timeline for submission of comments on this Consultation paper to SEBI is March 7, 2023. The highlights of proposed amendments in this Consultation paper are as follows:-

Sl.no	Reg no. / Subject	Nature	Proposed Amendment
1A	Point 5A Part A Para A of Schedule III – Disclosure of agreement	Insertion	**Disclosure And Approval Requirements For Certain Types Of Agreements That Bind Listed Entities:** In terms of regulation 30(6) read with clause 5 of para A of Part A of Schedule III of the LODR Regulations, agreements which are binding and not in the normal course of business have to be disclosed by a listed entity. The aforesaid requirement includes disclosure of shareholder agreements, joint venture agreements, family settlement agreements (to the extent that it impacts management and control of the listed entity), agreements with media companies etc. Revisions or amendments and termination of such agreements too have to be disclosed. Shareholder agreements are one of the common types of agreements entered into and disclosed by listed entities. A shareholder agreement (SHA) is an arrangement that regulates the relationship between the shareholders, the management of the company, ownership of the shares, rights, obligations, and protection of the shareholders. SHA may be entered into between shareholders (without the involvement of the company) or between the shareholder(s) and the company.

Sl.no	Reg no. / Subject	Nature	Proposed Amendment
			There have been instances wherein promoters have entered into binding agreements with third parties having an impact on the management or control of a listed entity or such agreements have placed certain restrictions on the listed entity. However, these facts were not disclosed to the listed entity and its shareholders. Non-disclosure of material information creates information asymmetry and results in significant market reaction when it is known to the public at large at a later stage. **Proposed Disclosure of agreements under regulation 30 of the LODR Regulations:** In order to cover disclosure of any agreement that impacts the management or control of a listed entity or imposes any restriction or creates any liability on a listed entity (irrespective of whether listed entity is a party to the agreement or not), it is proposed to introduce a new clause 5A in para A of part A of Schedule III of the LODR Regulations mandating disclosure of such agreements with effect from April 1, 2023. Further, agreements whose purpose and effect is to impact the management or control or impose any restriction or create any liability upon the listed entity also needs to be disclosed. However, agreements entered by a listed entity for the business operations of a company (eg. supply agreements, purchase agreements etc.) are proposed to be excluded from the scope of disclosures. **Existing and subsisting agreements, including whose purpose and effect is to impact management or control or impose any restriction or create any liability upon a listed entity:** The listed entity shall disclose existing and subsisting agreements as on March 31, 2023, to the stock exchanges under Regulation 30 of LODR Regulations on or before June 30, 2023.
1B	Schedule V – Disclosures in Annual Report	Insertion	**Disclosures in the Annual Report of a listed entity:** From April 1, 2023, the details of the aforesaid agreements entered during the financial year shall , in addition to disclosure requirements under regulation 30 read with Schedule III of the LODR Regulations, be disclosed in the Annual Report of the listed entity also (i.e., from FY 2023-24 onwards). This shall ensure availability of information about all such agreements at a single place for the shareholders and provides continuity of information to the shareholders.

Sl .no	Reg no. / Subject	Nature	Proposed Amendment
			Existing and subsisting agreements, including whose purpose and effect is to impact management or control or impose any restriction or create any liability upon a listed entity: The listed entity shall disclose all existing and subsisting agreements as on March 31, 2023 in the **Annual Report** of the listed entity for **FY 2022-23**.
1C	Obligation to inform listed entity	Insertion	**Obligation to inform the listed entity:** If the listed entity is not party to any agreement, it shall be obligatory on the part of the shareholders, promoters, promoter group, related parties, directors, key managerial personnel or any other officer of a listed entity or of its holding, subsidiary, associate company who are parties to such agreements to inform the listed entity about such agreements within 2 working days from the date entering into such an agreement. The listed entity, in turn, shall disclose the said details to the Stock Exchanges. **Existing and subsisting agreements, including whose purpose and effect is to impact management or control or impose any restriction or create any liability upon a listed entity:** If the listed entity is not party to any existing and subsisting agreement as on the date of this amendment becoming effective, it shall be obligatory on the part of the shareholders, promoters, promoter group, related parties, directors, key managerial personnel or any other officer of a listed entity or of its holding, subsidiary, associate company, who are parties to such agreements, to inform the listed entity about such agreements on or before May 31, 2023.
1D	Requirement to seek approval of Board of Directors and Shareholders	Insertion	**Board's opinion and Shareholder approval:** After notification of the amendments to the LODR Regulations, if any future agreement, whether or not the listed entity is party to such an agreement but excluding agreements entered into the normal course of business by a listed entity, imposes or has the effect of imposing any restriction or liability on a listed entity, the Board of Directors shall provide its opinion, along with detailed rationale, as to whether such an agreement is in the economic interest of the listed entity. The directors of the listed entity in consonance with their obligations of fiduciary nature are duty bound to assess the

Sl.no	Reg no. / Subject	Nature	Proposed Amendment
			agreement for ensuring that such an agreement is in the economic interest of the listed entity. Further, in order to provide an opportunity to the shareholders to evaluate the impact of such agreements, it is proposed that such agreements that have been entered or is proposed to be entered shall not be effective unless and until approved by the shareholders of the listed entity (approval through special resolution and 'majority of minority'). **Existing and subsisting agreements, including whose purpose and effect is to impact management or control or impose any restriction or create any liability upon a listed entity:** Board's opinion and ratification by shareholders of existing and subsisting agreements as on the date of this amendment becoming effective, needs to be taken in the first general meeting (AGM or EGM) of the listed entity held after April 1, 2023. It was observed that similar type of agreements, as discussed above, have been entered by promoter or promoter group earlier. It was also seen that information regarding such agreements being entered was not shared with board of directors of listed entity. Recently in two celebrated cases i.e pertaining to a large media group and one of the largest public sector bank, a similar disclosure lapse was seen.
2	Special rights to Pre-IPO shareholders/ Promoters	Insertion	**Review of special rights conferred to certain shareholders as per the AOA of a listed entity** To attract investments in a company prior to listing, special rights are offered by the company to its pre-IPO investors and the promoters. These special rights are included in the SHAs executed between the company and the pre-IPO investors / promoters. The range of these special rights varies across companies and depends on the specific requirement of the investor(s). Some of the common types of special rights are Nomination Rights, Veto Rights / Affirmative voting, Information Rights, Anti-Dilution Rights, Right of First Refusal, Tag Along Rights, Divestment Rights, etc.

MMJC

Sl.no	Reg no. / Subject	Nature	Proposed Amendment
			As per the principles specified in regulation 4 of the LODR Regulations, every listed entity shall ensure equitable treatment of all shareholders, including minority and foreign shareholders. Also, as per SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018 an issuer is required to provide a statement that the shares allotted in the public issue are equal in all respects, including dividends, with the existing shares issued by the company prior to the public issue, excluding SR (Superior Rights) equity shares. These special rights are placed in front of shareholders in the first general meeting after listing of shares for their approval. On a review of the voting pattern of public shareholders and the commentaries available in public domain around such special rights, it is observed that public institutional shareholders are increasingly voicing their concerns against special rights being conferred upon the promoters / founders / certain body corporates of those companies. Additionally, it is also observed that the SHAs are drafted in such a way that those special rights (nomination rights) would continue to be available even after significant dilution of their holding in those entities. This permits the shareholders to enjoy such special rights perpetually, which is against the principle of rights being proportional to one's holding in a company. Therefore, in order to address the issue of certain shareholders enjoying special rights perpetually, it is proposed that any special right (existing / proposed) granted to a shareholder of a listed entity shall be subject to shareholders approval once in every 5 years from the date of grant of such special rights. Further, the existing special rights available to shareholders shall be renewed within a period of 5 years from the date of notification of the amendments to the LODR Regulations.
3	Sale, disposal or lease of assets of a listed entity outside the 'Scheme	Insertion	**Sale, disposal or lease of assets of a listed entity outside the 'Scheme of Arrangement' framework** Presently sale, disposal or lease of whole or substantially the whole of the undertaking of the company OR where the company owns more than one undertaking, of the whole or substantially the whole of any of such undertakings happens either through Scheme of Arrangement (as prescribed in the Companies Act and / or the LODR Regulations and the circulars issued by SEBI) or outside the Scheme of

Sl .no	Reg no. / Subject	Nature	Proposed Amendment
	of Arrangement' framework		Arrangement framework, generally referred to as Business Transfer Agreement. Regulation 37 of LODR Regulations provides that the listed entities desirous of undertaking scheme of arrangement or involved in a scheme of arrangement shall file the draft scheme with Stock Exchange(s) for obtaining Observation Letter or No-objection Letter, before filing such scheme with any court or Tribunal. The objective of prior examination of scheme of arrangements by SEBI before filing with NCLT is that SEBI can ensure that rights of the minority shareholders are protected. SEBI, from time to time, has also issued various circulars/instructions which lay down the detailed requirements to be complied by listed entities while undertaking scheme of arrangements. One of the safeguards provided in case of slump sale through scheme of arrangements is requirement of taking 'majority of minority' approval from public shareholders. The extract of the provision mentioned in SEBI circular dated November 23, 2021 on 'Master circular on (i) Scheme of Arrangement by listed entities and (ii) relaxation under sub-rule (7) of rule 19 of SCRR 1957 also includes 'majority of minority' voting for cases where the scheme involves transfer of whole or substantially the whole of the undertaking of the listed entity and the consideration for such transfer is not in the form of listed equity shares. However, the sale, disposal or lease of the entire undertaking or substantial of the undertaking may also be executed outside the scheme of arrangement framework without being approved by NCLT. Such transactions will not be covered under the above-mentioned framework. To strengthen the extant framework of slump sale executed outside the scheme of arrangement framework, to safeguard the interest of minority shareholders and to align with the requirement, as applicable, under scheme of arrangement, the following proposals are made: 1. Introduction of provisions in LODR Regulations for sale, disposal or lease of whole or substantially the whole of the undertaking of the listed company or where the company

Sl.no	Reg no. / Subject	Nature	Proposed Amendment
			owns more than one undertaking, of the whole or substantially the whole of any one or more of such undertakings; 2. Mandating disclosure of the objects and commercial rationale for such sale, disposal or lease, to the shareholders; 3. Such sale, disposal or lease of whole or substantially the whole of the undertaking, of the listed company or where the listed company owns more than one undertaking, of the whole or substantially the whole of any of one or more such undertakings can be acted upon only if the votes cast by the public shareholders in favour of the proposal are more than the number of votes cast by the public shareholders against it. This shall be in addition to the requirement to pass a Special Resolution as provided in section 180(1)(a) of the Companies Act, 2013.
4	Board Permanency In Listed Entities / need for periodic review	Insertion	SEBI has noted the following: a) Not all directors serving on the board of listed entity may be subject to 'retirement by rotation'. b) There may be some directors who are appointed to the board of a listed entity without a defined tenure and not liable to 'retirement by rotation'. c) In addition to the above, by virtue of the provisions of the AoA of a company, a person can be appointed as a director on a "permanent- basis". Such director, so appointed on the basis of the provisions of AoA, serves as a "permanent-director" on the board of the company. Consequently, the shareholders of listed entities do not get an opportunity to evaluate the performance of such directors appointed in the aforesaid manner and thereby enjoying "board permanency", disregarding the intent of shareholders on continuation of such directors on the board of a listed entity. Proxy advisors have also been raising concerns with respect to these kind of directorships in the companies. Recently in a dispute between two major corporates arising out control over a media company, these categories of directorships was posing problem for change in control. SEBI expressed a view that in the interest of good corporate governance at listed entities, all directors appointed to the board of a listed entity need to go through periodic

Sl .no	Reg no. / Subject	Nature	Proposed Amendment
			shareholders' approval process, thereby providing legitimacy to the director to continue to serve on the board. Therefore, on the similar lines being followed in the appointment / re-appointment of MD / WTD and IDs, it seems necessary that the directorship of any individual serving on the board of a listed entity should be subject to periodic shareholders' approval at least once in every five years from the date of his / her first appointment to the board. It is proposed that from March 31, 2024, if there is any director serving on the board of a listed entity without his / her appointment or re-appointment being subject to shareholders' approval during the last 5 years i.e., from April 1, 2019, the listed entity shall take shareholders' approval in the first general meeting to be held after April 1, 2024, for his / her continuation on the board of the listed entity. From April 1, 2024, subject to the other applicable provisions of law, the listed entity shall ensure that the directorship of all directors serving on the board or appointed to the board is put up to shareholders for approval at least once in every 5 years. The aforesaid provisions would not be applicable to appointed pursuant to the orders of a Court or a Tribunal director. Recently in a tussle between large media company and one of the biggest private sector banks regarding gaining control over the media company by way of controlling the composition of board of directors of media company, permanent board memberships of promoter director of media company was proving hindrance. This point was widely discussed at before various authorities and matter was also referred to SEBI.

The link for this Consultation Papers is given below

https://www.sebi.gov.in/reports-and-statistics/reports/feb-2023/consultation-paper-on-strengthening-corporate-governance-at-listed-entities-by-empowering-shareholders-amendments-to-the-sebi-lodr-regulations-2015_68261.html

SEBI Consultation paper on review of Corporate Governance norms for High Value Debt Listed Entities dated February 08, 2023

BACKGROUND:

Securities and Exchange Board of India (SEBI) had introduced the concept of High Value Debt Listed Entity (HVDLE) by amending SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (LODR) vide notification dated September 07,2021. An HVDLE is an entity which has listed its non-convertible debt securities on a recognised stock exchange and has an outstanding principal value of listed non-convertible debt securities of Rs. 500 Crore and above. Corporate Governance norms specified in LODR were also made applicable to HVDLE through the aforementioned amendment on 'comply and explain basis' until March 31, 2023 and on mandatory basis thereafter.

In order to regulate all the RPTs and with a view to ensure protection of the interest of the debenture holders as they are also the lenders of the Company, SEBI has come up with a consultation paper pertaining to review of Corporate Governance norms for a High Value Debt Listed Entity. It was open for public comments till February22, 2023.

A) REGULATION 15(2) OF LODR – APPLICABILITY OF CORPORATE GOVERNANCE PROVISIONS

The corporate governance norms become applicable to HVDLE once its non-convertible debt securities are listed on a recognised stock exchange and have an outstanding principal value of listed non-convertible debt securities of Rs. 500 Crore and above. As per Regulation 3(3) of LODR, the corporate governance norms shall continue to remain applicable to a HVDLE even if the value of outstanding listed debt securities falls below the prescribed limit. However, in case of entities who have their specified securities listed on Stock exchanges, corporate governance norms remain applicable only till a period of three consecutive financial years from the time such listed entities fall below the specified threshold.

An alignment, in terms of period of applicability of corporate governance norms to HVDLEs in line with that of listed entities that have their specified securities listed, is now proposed through means of this consultation paper. It is proposed that once the regulations become applicable to a HVDLE, they shall continue to remain applicable till such time the outstanding value of listed non-convertible debt securities of such entity reduces and remains below the specified threshold for a period of three consecutive financial years.

B) EXISTING APPROVAL MECHANISM UNDER REGULATION 23(4) OF LODR:

SR. NO	TYPE OF TRANSACTION	APPROVAL ROUTE*
1.	All Material RPTs	Prior shareholder's approval
2.	Subsequent Material modifications as defined by the Audit Committee	Prior shareholder's approval
3.	Material RPTs where listed subsidiary is a party but listed entity is not a party and where Regulation 23 and 15(2) are applicable to the listed subsidiary	No prior shareholder's approval required by listed entity
4.	Material RPTs entered by unlisted subsidiaries of a listed subsidiary	Prior approval of the shareholders of the listed subsidiary
5.	Mateiral RPTs entered by unlisted subsidiaries of listed holding entity	Prior approval of the shareholders of the listed holding entity

no related party shall vote to approve such resolutions whether the entity is a related party to the particular transaction or not.

CHALLENGES FACED BY HVDLE:

The difficulty in transacting RPTs where shareholder's approval is required, as represented by HVDLEs whose equity shares are unlisted, is that the shareholding in HVDLEs is concentrated i.e. the shares are wholly/substantially held by one or few shareholders and all of them are related parties. This makes it impossible for them to take approval from shareholders for RPTs as all shareholders fall in the definition of Related Parties and cannot vote to approve such RPT.

COURSE OF ACTION SUGGESTED BY SEBI:

SEBI has analysed the issue pertaining to HVDLEs 'impossibility of compliance' in relation to shareholders approval to be sought for RPT transactions and has come up with the following course of action. This shall be applicable only to those HVDLEs who have only listed their non-convertible debt securities listed and have 90% or more of the shareholders in number as related parties:

1. A copy of agenda of General Meeting where an item pertaining to RPT is proposed will also be shared with the debenture holders holding listed non-convertible debt securities ('debenture holders').
2. The Debenture holders shall submit their objections in writing or through electronic mode at the Company's dedicated functional email ID within 7 days from the dispatch of the agenda item.
3. If 'objections' are received from the debenture holders holding 75% or more in value, based on number of responses received, then the Board of Directors shall withdraw the RPT agenda.

4. All shareholders, including the Related Parties can vote on such RPTs. (SEBI has considered third proviso of Section 188(1) of the Companies Act, 2013 for granting this exemption.)

CERTIFICATION BY A PRACTICING COMPANY SECRETARY (PCS):
A PCS has to examine the responses received from the Debenture holders and issue a certificate within 3 days from the last day by which responses from the debenture holders are to be received. The certificate should contain a log of total responses received, number of objections and no-objections received. In case there are no responses received, a certificate mentioning the same is also to be issued by the PCS.

The certificate shall be disseminated promptly on the website of the company, the website of the Stock Exchanges, the website of the Debenture Trustee and sent by email to the shareholders and to the debenture holders.

ANOMALY:
As per section 71(2) of the Companies Act, 2013, "No company shall issue debentures carrying voting rights." This means the debenture holders will not have voting rights on any matter with regard to the company.

Whether giving this right to debenture holders, for giving consent or raising objections on material RPTs which are put up for voting by shareholders, will it not mean that voting rights are being given to debenture holders? Whether this shall be in compliance of the provisions of Companies Act, 2013?

If this proposal is approved by SEBI, then it can lead to a situation where shareholders might exercise their voting rights and approve the resolution. However, one or more debenture holder who may be holding 75% or more in value of debentures may object to the resolution.
In such situation, the shareholders – who are the owners of the company would have approved the RPT, considering that it is in the interest of company to go ahead with that RPT. But the debenture holders – who are lenders, and do not have any voting rights as per Companies Act, 2013, have raised objection and the entire transaction will have to be withdrawn by the board of directors!!!

CONCLUSION:
The entire purpose of bringing out this Consultation Paper was to provide a solution to the 'impossibility of voting' by shareholders, other than related parties, on material RPTs by HVDLE where all the shareholders were related parties. The exemption proposed to be given for voting by shareholders, if more than 90% in number are related parties, in line with the third proviso to sec 188(1) shall serve this purpose.

However, giving a right to debenture holders, to object on a material RPT, may not be always in the interest of the company. This right to object for an RPT is not given even to bankers who are giving loans to company by pooling the funds of public, whereas debenture holder is an investor who would be investing his personal money by subscribing to debentures. Hence, giving this right to object to debenture holders may be prone to misuse by some big players and this may not be in the best interest of the HVDLE.

Clarification by SEBI to first time issue of NCDs w.r.t amendment in Articles of Association

I. Introduction:

Securities and Exchange Board of India ("SEBI") has, by its **circular dt: February 9, 2023,** provided a relief to first time issuers of non-convertible debentures ("NCD") to amend their Articles of Association, for inserting timeline for appointment of director nominated by debenture trustees as required under the newly amended Regulation 23(6) of SEBI (Issue and Listing of Non-Convertible Securities) Regulations, 2021 ("ILNCS Regulations"), within 6 months of listing and not immediately before listing**.**

II. Background of Amendment in ILNCS Regulations:

SEBI had vide an amendment dated February 2, 2023 amended Regulation 23(6) of ILNCS Regulations to the effect that if an issuer of NCDs is a company, it shall ensure that its Articles of Association has a clause to require its Board of Directors to appoint the person nominated by the debenture trustee in the terms of clause (e) of sub-regulation (1) of regulation 15 of SEBI (Debenture Trustee) Regulation 1993 as a Director on its Board. **For existing issuers** whose NCDs are outstanding and listed as on date of this amendment had been mandated to amend its Articles of Association, if necessary to comply with this provision, **on or before September 30, 2023**. The timeline of 1 month for appointment of such nominee director is also prescribed to be included in the Debenture Trust Deeds by existing issuers by September 30, 2023.

III. Anomaly:

The amended provision provided a timeline till September 30, 2023 to alter Articles of Association, for existing issuers whose NCDs are already listed. Question had arisen that what will be the timeline for amending the Articles of Association with respect to those issuers who would be in the process of issuing NCDs and the NCDs were to be listed post February 2, 2023? Will they also get time of six-seven months to comply with this or they have to comply with immediate effect i.e. prior to listing of NCDs?

Various representations were made by market participants to SEBI, who are in the process of listing their private or public NCDs, to provide a time frame, as provided to already listed issuers, to amend their Articles of Association since it requires formalities like approval from shareholders and need to follow the timelines given in Companies Act, 2013 for conducting board and general meetings and this may delay the process of NCD listing.

IV. Clarification:

Hence, SEBI has now clarified that Stock Exchanges are advised to take an undertaking from such first - time issuers that they will **ensure that their Articles of Association are amended within a period of six months from the date of the listing** of the NCDs. This undertaking will be obtained by stock exchanges at the time of granting the in - principle approval. The issuer shall, within such time, comply and report compliance to Stock Exchanges, which shall periodically monitor/ remind such issuers on doing the needful.

Copy of circular can be accessed at below link:
https://www.sebi.gov.in/legal/circulars/feb-2023/clarification-in-respect-of-the-compliance-by-the-first-time-issuers-of-debt-securities-under-sebi-issue-and-listing-of-non-convertible-securities-regulations-2021-with-regulation-23-6-_67936.html

Order of the SEBI Adjudicating Officer
Adjudication Order in the matter of Complaint by Pushpaben Rasiklal Patel.

Facts of the case:

1. SEBI had received a complaint from Ms. Pushpaben Rasikbhai Patel ('Genuine Shareholder') on August 12, 2021 regarding fraudulent transfer of shares and duplicate issuance of shares to the person who is not a real owner of the equity shares of Swiss Glasscoat Equipment Limited (name changed to HLE Glascoat Limited) (hereinafter referred to as ***"Company"/ "Noticee 1"***). Link Intime India Pvt. Ltd. (hereinafter referred to as ***"Noticee 2"***) is the Registrars and Share Transfer Agents of the company. Noticee 1 began process of change of RTA from MCS Ltd to Noticee 2 by entering into MOU on January 2016. Process of transfer of RTA got converted in March 2016. It was alleged by Noticee 2 that there were lapses by MCS while transferring data relating to shareholders' folio. This was a technical error as the data was not in specified data format as alleged by Noticee 2.

2. The fraudulent activity began when on October 1, 2016, Noticee 2 received a letter from a Pushpaben Rajendrabhai Patel (non-genuine shareholder) residing at 'B – 19, Karelibaug Society, Behind Bright School, Karelibaug, Vadodara – 390018' stating that she had not received dividend for the year 2015-16. Non-genuine shareholder also submitted that she had misplaced share certificates in respect of 300 shares of Noticee 1. Accordingly, non-genuine shareholder was advised to submit acknowledged copy of the Police Complaint, Indemnity Bond on Rs.200/- stamp paper, Affidavit on Rs.100/- stamp paper, copy of PAN and Aadhar card and signature verification done by the banker. Vide letter dated November 11, 2016 non-genuine shareholder submitted all the relevant documents. In this regard, Noticee 2 wrote to Bombay Stock Exchange Limited (hereinafter referred to as ***"BSE"***) with a copy to National Stock Exchange (hereinafter referred to as ***"NSE"***) to display the information regarding misplaced shares and to refrain trading in those shares and informed Noticee 1 of the same. Later,

on December 5, 2016 duplicate shares were issued based on the documents received.

3. Further, Noticee 1 vide letter dated January 12, 2017, informed her that the address mentioned by her is different from that registered with Noticee 1 and also, advised her to submit an application for change in address along with bank attested supporting documents such as driving licence, bank statement, self- attested copy of PAN card etc. Accordingly, she submitted all the relevant documents and vide letter dated January 18, 2018. Noticee 2 informed her regarding the change in address vide letter dated January 25, 2017. The physical share certificates held by the Non-genuine Shareholder were dematerialised on January 30, 2017. Subsequently, in November 2018, genuine shareholder had requested Noticee 2 for dematerialization of her shares and her request was rejected. She then, vide letter dated May 26, 2021 wrote to Noticee 1 regarding rejection of request of dematerialization of the said shares and non-receipt of share certificates. Noticee 1, vide letter dated July 13, 2021 informed Pushpaben Rasiklal Patel that duplicate share certificates for 300 shares had already been issued and dematerialized on January 30, 2017. Later on, she filed a complaint with SEBI on August 12, 2021 in which she inter alia, stated that 300 equity shares held by her had fraudulently been transferred to someone else and the Company and Link Intime India Pvt. Ltd. (collectively known as the "Noticees") are not investigating in the matter and are providing unsatisfactory replies with irrelevant documentary proof which does not belong to the real shareholder.

4. In view of the same, adjudication proceedings is initiated in respect of Noticee 1 for alleged violation of Instructions to Registrars To An Issue /Share Transfer Agents dated October 11, 1994 and non-compliance with clause 23 SEBI of Circular dated May 9, 2001 and Noticee 2 for the alleged violation of clause 3 of Code of Conduct under Schedule III of Regulation 13 of SEBI (Registrars to an Issue and Share Transfer Agents) Regulations, 1993 (hereinafter referred to as "RTI STA Regulations") and non-compliance with clause 23 of SEBI Circular dated May 9, 2001.

Arguments by Noticee 2:

1. **Demat of shares in fraudulent manner:** As discussed above this matter was initiated with a complaint by Genuine Shareholder on SCORES platform

stating that 300 equity shares had fraudulently been transferred to someone else. Further, it was highlighted that Noticee 1 and Noticee 2 are not properly investigating the matter and giving same replies again and again. On investigation it was found that there were two different persons with same name and surname but different middle names residing in same vicinity. As noted above genuine shareholder and non-genuine shareholder both were having common address of "Behind Bright School, VIP Road, Karelibaug, Vadodara" The only difference was of their names of buildings viz. genuine shareholder was residing at 262, Ainath society, Behind Bright School, VIP Road, Karelibaug, Vadodara and non-genuine shareholder was 'B-19, Karelibaug Society, Behind Bright School, VIP Road, Karelibaug, Vadodara'. Noticee 1 received complaint from non-genuine shareholder regarding non-receipt of dividend warrant and issue of duplicate share certificate. Noticee 1 and Noticee 2 on fulfilling all the requisite procedures dispatched warrants and duplicate share certificates on January 25, 2017. These shares were further dematerialized by non-genuine shareholder on January 30, 2017. Noticee 1 came to know about this fraudulent act when genuine shareholder requested for demat of shares in November 2018. Noticee 1 rejected her request stating that the shares were already demat. Post this there was no reply from genuine shareholder for three years and in August 2021 she filed a complaint with SEBI through SCORES. On investigation Noticee 1 could locate the non-genuine shareholder and filed a police complaint for fraud under relevant provisions of Indian Penal Code. Non-genuine shareholder stated that all these acts were undertaken by her husband who is a stockbroker. Non-genuine shareholder further agreed to pay the damages to the genuine shareholder. Later on, in spite of various follow ups, non-genuine shareholder did not turn up for payment of damages. Later on, Noticee 1 entered into a settlement agreement and paid lumpsum amount of Rs 10,30,000/- to genuine shareholder.

2. **It did exercise proper due diligence while transferring data from erstwhile RTA i.e. MCS Ltd:**
   a. Noticee 2 submitted that the database files provided by the erstwhile RTA, MCS Ltd. to Noticee 1, HLE Glascoat were in a dBASE. DBF file structure customized and maintained (.dbf file is a database file used by dBASE, a database management system application in a customized version by each user basis their features and capabilities). Noticee 2 further submitted that data structure provided by MCS Limited pertaining to this shareholder, Pushpaben R. Patel, was not in the standard format resulting in an error at the time of conversion wherein the first line of the address of the shareholder was not converted/ populated in Noticee 2's system. Since then, this data has been updated / overwritten in the software with the passage of time by Noticee 2, due to its due diligence from time to time.

b. Noticee 2 further submitted that as far as the request for change in address is concerned, as per the data received from the MCS Ltd, the registered address under the subject folio was only 'Behind Bright School, VIP Road, Karelibaug, Vadodara'. Noticee 2 further highlighted that it received complaint of non-receipt of dividend warrant from Pushpaben Rajendrabhai Patel ('non-genuine shareholder') on October 1, 2016. In the same letter Noticee 2 was requested to issue duplicate share certificates to her, pursuant to the loss of original share certificates. Noticee 2 informed the Applicant (non-genuine shareholder) about the procedure for issue of duplicate share certificate and documents to be submitted in relation to the same. On receipt of requisite documents, Noticee 2 dispatched the duplicate share certificate on the address as mentioned in the subject folio in its records (and not the address written on the letter by the non-genuine shareholder which was a detailed address). But the letter was returned undelivered with a remark *'Short Address'*. The non-genuine shareholder contacted the representative of Noticee and informed that the address registered with Noticee 1 & 2was different than her actual address and enquired the procedure to change address. Noticee 2 further stated that before changing the address of the shareholder in the records, Noticee 2 sought and obtained all the requisite documents, including the application for change in address, bank attested supporting documents such as driving license, bank statement, self-attested copy of PAN, etc. The Non-genuine Shareholder submitted bank statement of Dena Bank and a copy of Aadhaar, which mentioned the new address, viz. 'B-19 Karelibaug Society, Behind Bright School, VIP Road, Vadodara – 390018'. It is only after carrying out these checks that the address was updated in the records of Noticee 2. Noticee 2 further submitted that MCS Ltd (erstwhile RTA) did not have PAN number and signature.

c. Further Noticee 2 submitted that with respect to issuance of duplicate share certificates, at the time of issuance of duplicate share certificates to the Non-genuine Shareholder, all the requisite documents were sought for and obtained, including Indemnity Bond, Notarised affidavit, acknowledged copy of police complaint, self-attested copy of PAN, self-attested copy of Aadhaar, etc. Noticee 2 further submitted that they wrote to the stock exchanges requesting them to display the claim of the non-genuine shareholder and inform investors to refrain from trading in said shares. It was only after these conditions were met that Noticee 2 issued duplicate share certificate. Further, Noticee 2 stated that they were responsible to verify the documents provided and not validate them at the time of due diligence. In the present instance, it is no one's case that the documents furnished by the non-genuine shareholder were fake.

Noticee 2 further stated that they processed the request only after all these documents were obtained which were issued by police / bank / validated by notary. Noticee 2 highlighted that they had no reason to suspect that the documents submitted by the non-genuine shareholder which included FIR/Acknowledged copy of police complaint for loss of share certificates, indemnity bond, banker verification form, identity proofs or address proofs which were received by it in 2016 were not genuine or were received through misrepresentation.

d. As an RTA, the only process by which Noticee 2 could carry out its obligation was by verifying the genuineness of the documents submitted by the Non-Genuine Shareholder. As long as this obligation was duly discharged, the Noticee 2 cannot be held liable for the validity or otherwise of the submitted supporting documents. Noticee 2 further submitted that there were no documents whatsoever that were handed over to Noticee 2 by the erstwhile RTA, i.e., MCS Limited or by Noticee 1, viz. HLE Glascoat Limited pertaining to the investor Pushpaben Rasiklal Patel. Noticee 2 submitted that it shall not be held liable for any alleged violations in respect of the obligation under Clause 23 of the 2001 Circular.

3. **Matter was referred to SEBI post limitation period:** The present proceedings arise from a SCORES complaint filed by the complainant in respect of cause of action that, by SEBI's own Show Cause Notice (SCN), arose in December 2016 - January 2017. The complainant filed the complaint with SEBI on August 12, 2021, i.e. 5 years after the cause of action arose. SEBI's FAQ prescribe a period of limitation for initiating proceedings. The FAQs prescribe a clear, specific and unambiguous period of limitation. It provides that cause of action should arise within 1 year from the date of complaint. In the present instance, the complaint, which forms the foundation of the present proceedings, was barred by the limitation. Accordingly, issuance of the SCN and continuing thereupon is barred by limitation unless specific jurisdiction is provided to the Ld. Adjudicating Officer, the same cannot be considered by SEBI / Ld. Adjudicating Officer solely based on the representations made by the complainant.

Arguments made by SEBI:

1. **Demat of shares in fraudulent manner:** SEBI, on understanding the facts of the case, noted that Noticee 1 and Noticee 2 had taken various steps to resolve the complaint filed by Pushpaben Rasiklal Patel. In order to

protect the interest of the investor, Noticee 1 also entered into a settlement agreement with Pushpaben Rasiklal Patel (genuine shareholder) and paid lump sum consideration of Rs.10,30,000/- as full and final settlement of all the claims. Pursuant to the settlement claim, the complaint filed by Pushpaben Rasiklal Patel has also been withdrawn. Hence, the issue stands addressed.

2. **It did exercise proper due diligence while transferring data from erstwhile RTA i.e. MCS Ltd**: SEBI noted that on January 30, 2016, a Memorandum of Understanding (hereinafter referred to as "**MoU**") was executed between Noticee 1 and Noticee 2 whereby Noticee 2 became the Share Transfer Agent (hereinafter referred to as "**STA**") of Noticee 1. Prior to this, one MCS Limited was the STA of Noticee 1. Pursuant to the execution of the current MoU, the database file pertaining to Noticee 1 was transferred to it by MCS Ltd. who in turn handed it over to Noticee 2. SEBI noted that while converting/ migrating the data pertaining to Pushpaben R Patel, due to an error, the first line of the address was not converted in Noticee 2's system. While MCS Ltd. acted as the STA, the correct address was available with it as the equity dividend warrant dated October 1, 2015 was sent by Noticee 1 to Pushpaben R (Rasiklal) Patel at '*262 Ainath Society, Behind Bright School, VIP Road, Karelibaug, Baroda*' which was the correct address. Noticee 2 submitted that while migrating the data into their system, error occurred and the full address was not imported. Noticee 2 further submitted that the data structure provided by MCS Limited was not in the standard format. However, Noticee 2 did not clarify what is standard format. Hence the submission of Noticee 2 is not acceptable. It is observed that Noticee 2 failed to oversee the proper migration of data from the record of the previous STA to its system. Being the STA, it is expected that Noticee 2 should have taken more care in ensuring the correct details of the shareholders are migrated from the database of the previous STA to its own database. In view of the above, SEBI found that Noticee 2 has failed to exercise due diligence and the allegation of violation of clause 3 of Code of Conduct under Schedule III of Regulation 13 of RTI STA Regulations by Noticee 2 stands established. As per 'Instructions to Registrars To An Issue /Share Transfer Agents' dated October 11, 1994, the company is primarily responsible for the work of the STA. But in this case SEBI stated that, Noticee 1 transferred the CD to Noticee 2 as received from MCS Limited. SEBI further stated that it was not reasonably possible for Noticee 1 to ensure that the complete data pertaining to all the shareholders has properly migrated from the system of the erstwhile STA to Noticee 2. In view of the same, I find that the allegation of the violation of 'Registrars To An Issue /Share Transfer Agents' dated October 11, 1994 by Noticee 1 does not stand established. SEBI accepted the contention of the Noticee 2 that due to non-availability of PAN and signature it was not possible for RTA to verify.

3. **Matter was referred to SEBI post limitation period:** As per the FAQs on SCORES issued by SEBI, "…the complaint shall be lodged on SCORES within one year from the date of cause of action." One of the main reasons for the establishment of SEBI is protection of investors. In such a case, SEBI cannot overlook the plight of the investor only because it had not followed the timeline stated in the FAQ. Moreover, FAQ is merely a guidance given by SEBI for the benefit of the market. SEBI always reserves the right to reject or examine any complaint lodged on SCORES. Further, the FAQ quoted by Noticee 2 became operational from December 2022. During the relevant period, the FAQ read as "From 1st August, 2018, an investor may lodge a complaint on SCORES within three years from the date of cause of complaint." In the present case, Pushpa Rasiklal Patel had requested for dematerialization of shares on November 2018 which was rejected and she was informed that duplicate shares were issued on November 28, 2016 and dematerialised on January 30, 2017. She filed a complaint with SEBI on August 12, 2021. So, it is clear that complaint has been filed well within a period of three years.

Held: Penalty of Rs 1,00,000 on Noticee 2 under the provisions of section 15HB of the SEBI Act for not exercising proper due diligence and care (in ensuring that all relevant data about all shareholders was duly collated and available with them like the first line of address).

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