



SEBI Board Meeting

The SEBI Board met in Mumbai today and took the following decisions:

I. Framework for Issuance of Differential Voting Rights (DVR) Shares

There is an increasing debate about the need to enable issuance and listing of shares with differential voting rights, commonly known as DVRs in India. Such shares have rights disproportionate to their economic ownership.

The Board approved a framework for issuance of differential voting rights shares along with amendments to the relevant SEBI Regulations to give effect to the framework.

The key proposals approved are as follows:

1. *Eligibility:* A company having superior voting rights shares (SR shares) would be permitted to do an initial public offering (IPO) of only ordinary shares to be listed on the Main Board, subject to fulfillment of eligibility requirements of the SEBI(Issue of Capital and Disclosure Requirements) Regulations, 2018 and the following conditions:
 - i) The issuer company is a tech company (as per the definition in Innovators Growth Platform) i.e. intensive in the use of technology, information technology, intellectual property, data analytics, bio-technology or nano-technology to provide products, services or business platforms with substantial value addition.
 - ii) The SR shareholder should be a part of the promoter group whose collective net worth does not exceed Rs 500 Crores. While determining the collective net worth, the investment of SR shareholders in the shares of the issuer company shall not be considered.
 - iii) The SR shares have been issued only to the promoters/ founders who hold an executive position in the company.

- iv) The issue of these SR shares has been authorized by a special resolution passed at a general meeting of the shareholders.
 - v) SR shares have been held for a period of at least 6 months prior to the filing of Red Herring Prospectus (RHP).
 - vi) SR shares have voting rights in the ratio of minimum 2:1 to maximum 10:1 compared to ordinary shares.
2. *Listing and Lock-in:* SR shares shall also be listed on Stock Exchanges after the issuer company makes a public issue. However, SR shares shall be under lock-in after the IPO until their conversion to ordinary shares. Transfer of SR shares among promoters shall not be permitted. No pledge/ lien shall be allowed on SR shares.
3. *Rights of SR shares:* SR shares shall be treated at par with the ordinary equity shares in every respect, including dividends, except in the case of voting on resolutions. The total voting rights of SR shareholders (including ordinary shares), post listing, shall not exceed 74%.
4. *Enhanced corporate governance:* Companies having SR shareholders shall be subject to enhanced corporate governance as follows:
- i) At least $\frac{1}{2}$ of the Board and $\frac{2}{3}$ rd of the Committees (excluding Audit Committee) as prescribed under SEBI (LODR) Regulations, 2015 shall comprise of Independent Directors.
 - ii) Audit Committee shall comprise of only Independent Directors.
5. *Coat-tail Provisions:* Post-IPO, the SR Equity Shares shall be treated as ordinary equity shares in terms of voting rights (i.e. one SR share shall have only one vote) in the following circumstances:
- i) Appointment or removal of independent directors and/or auditor;
 - ii) In case where promoter is willingly transferring control to another entity
 - iii) Related Party Transactions in terms of SEBI(LODR) Regulations involving SR shareholder
 - iv) Voluntary winding up of the company;

- v) Changes in the company's Article of Association or Memorandum - except any changes affecting the SR instrument
 - vi) Initiation of a voluntary resolution plan under IBC;
 - vii) Utilization of funds for purposes other than business
 - viii) Substantial value transaction based on materiality threshold as prescribed under LODR;
 - ix) passing of special resolution in respect of delisting or buy-back of shares; and
 - x) Any other provisions notified by SEBI in this regard from time to time.
6. *Sunset Clauses*: SR shares shall be converted into ordinary shares in following circumstances/ events:
- i) Time Based: The SR shares shall be converted to Ordinary Shares on the 5th anniversary of listing. The validity can be extended once by 5 years through a resolution. SR shareholder would not be permitted to vote on such resolutions.
 - ii) Event Based: SR shares shall compulsorily get converted into ordinary shares on occurrence of certain events such as demise, resignation of SR shareholders, merger or acquisition where the control would be no longer with SR shareholder, etc.
7. *Fractional Rights Shares*: Henceforth, issue of fractional rights shares by existing listed companies shall not be allowed. The need for allowing issue of fractional rights shares by listed companies may however be reviewed after gaining enough experience with the use of SR shares.

The Board, while approving the amendments, considered the recommendations of the Primary Market Advisory Committee (PMAC) and the public comments on the Consultation Paper.

II. Amendments to SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 - payment relating to royalty and brand usage

1. SEBI (Listing Obligations and Disclosure Requirements) Regulations had prescribed that payments made to related parties towards brand usage or royalty are to be considered material if the transaction(s) exceed 2% of the annual consolidated turnover of the listed entity during a financial year. This required

approval of the shareholders, with no related party having a vote to approve such resolutions. This provision was to come into effect from April 1, 2019. In view of the representations received on the subject and with a view to analyse them, the Board had decided to defer the implementation of this provision for three months i.e. till June 30, 2019.

2. The Board has now, after considering the representations, decided that payments made to related parties towards brand usage or royalty may be considered material if the transaction(s) exceed 5% of the annual consolidated turnover of the listed entity during a financial year and would require approval of the shareholders, with no related party having a vote to approve such resolutions.

III. Disclosure of Encumbrances

The Board has approved the following proposals:

1. The term “encumbrance” as defined in the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 shall henceforth include, -
 - i) any restriction on the free and marketable title to shares, by whatever name called, whether executed directly or indirectly;
 - ii) pledge, lien, negative lien, non-disposal undertaking;
 - iii) any covenant, transaction, condition or arrangement in the nature of encumbrance, by whatever name called, whether executed directly or indirectly.
2. Promoters shall be required to disclose separately detailed reasons for encumbrance whenever the combined encumbrance by the promoters and persons acting in concert (PACs) crosses 20% of the total share capital in the company or 50% of their shareholding in the company. The stock exchanges will maintain the details of such encumbrance along with purpose of encumbrance, on their websites.
3. The promoters shall be required to declare to the audit committee of the company and to the stock exchanges on a yearly basis, that they along with PACs, have not made any encumbrance directly or indirectly, other than already disclosed, during the financial year.

The Board has taken the above measures in the context of recent concerns w.r.t. promoter/ companies raising funds from Mutual Funds/ NBFCs through structured

obligations, pledge of shares, non-disposal undertakings, corporate/ promoter guarantees and various other complex structures.

IV. Review of Risk Management Framework of Liquid Funds, Investment Norms and Valuation of Money Market and Debt Securities by Mutual Fund

In light of a few credit events in the fixed income market that led to increase in liquidity risk of Mutual Funds, a need was felt to review the regulatory framework and take necessary steps to safeguard the interest of investors and maintain the orderliness and robustness of Mutual Funds.

In this context, SEBI had constituted working groups representing AMCs, industry and academia to review the risk management framework with respect to liquid schemes and to review the existing practices on valuation of money market and debt securities. Further, an internal working group within SEBI was constituted to *inter-alia* review norms for Mutual Funds for investment in various debt and money market securities.

The analysis along with recommendations of the working groups were placed in a meeting of Mutual Fund Advisory Committee (MFAC). In this regard, MFAC made several recommendations.

The Board after deliberations, *inter-alia*, approved the following proposals:

Risk Management Framework of Liquid Funds and prudential norms governing investments in debt and money market instruments

1. Liquid Schemes shall be mandated to hold at least 20% in liquid assets such as Cash, Government Securities, T-bills and Repo on Government Securities.
2. The cap on sectoral limit of 25% shall be reduced to 20%. The additional exposure of 15% to HFCs shall be restructured to 10% in HFCs and 5% exposure in securitized debt based on retail housing loan and affordable housing loan portfolios.
3. The valuation of debt and money market instruments based on amortization shall be dispensed with completely and shall be based on mark to market.

4. Liquid and overnight schemes shall not be permitted to invest in Short Term Deposits, debt and money market instruments having structured obligations or credit enhancements.
5. A graded exit load shall be levied on investors of liquid schemes who exit the scheme upto a period of 7 days.
6. Mutual Fund schemes shall be mandated to invest only in listed NCDs and the same would be implemented in a phased manner. All fresh investments in Commercial Papers (CPs) shall be made only in listed CPs pursuant to issuance of guidelines by SEBI in this regard.
7. All fresh investments in equity shares by Mutual Fund schemes shall only be made in listed or to be listed equity shares.
8. Prudential limits on total investment by a Mutual Fund scheme in debt and money market instruments having credit enhancements and on investment by Mutual Fund scheme in such debt securities of a particular group, as percentage of debt portfolio of the respective scheme have been prescribed at 10% and 5% respectively.
9. There should be adequate security cover of at least 4 times for investment by Mutual Fund schemes in debt securities having credit enhancements backed by equities directly or indirectly.

Valuation of Money Market and Debt Securities by Mutual Funds

1. In order to make existing provisions on valuation of money market and debt securities more reflective of best practices, various proposals for amending the extant provisions were approved.
2. Further, in order to bring uniformity and consistency in valuation, various proposals on the waterfall approach for valuation of non-traded money market and debt securities by Mutual Funds were approved, along with acknowledging that valuation agencies may need a certain degree of flexibility in order to ensure fair pricing of securities. Nevertheless, in terms of the Principles of Fair Valuation, AMCs are responsible for ensuring fairness of valuation and they may deviate from the valuation guidelines, subject to appropriate documentation and disclosure.
3. In order to increase the robustness of valuation and address possible mis-use, various proposals related to valuation of Inter-scheme Transfers (ISTs), disallowing the use of own trades for valuation etc., were approved.

Suitable grandfathering wherever applicable and adequate time period shall be provided for implementation of the above proposals.

V. Amendments to SEBI (PIT) Regulations

The Board considered representations received from the market on certain aspects relating to Code of Conduct prescribed in the SEBI (Prohibition of Insider Trading) Regulations, 2015 (PIT Regulations).

Upon consideration, the Board approved amendments clarifying that trading window closure for listed companies shall be applicable from end of every quarter till 48 hours after declaration of financial results. The amendments clarify that such closure shall not be applicable in respect of transactions such as off-market inter-se transfer between insiders, transaction through block deal window mechanism between insiders, transaction due to statutory or regulatory obligations, exercising of stock options, pledging of shares for bona fide transaction such as raising of funds and transactions for acquiring shares under further public issue, right issue and preferential issue, exercising conversion of warrants / debentures, tendering shares under buy-back, open offer and delisting etc. under respective regulations, subject to conditions specified. The Board also approved amendments clarifying material financial relationships.

VI. SEBI Annual Report: 2018-19

The Board considered and approved the SEBI Annual Report: 2018-19. In compliance with Section 18(2) of SEBI Act, 1992, the Annual Report would be submitted to the Central Government.

Mumbai

June 27, 2019