

NANGIA & CO LLP

CHARTERED ACCOUNTANTS



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Foreword

India has emerged as the fastest growing major economy in the world and is expected to be one of the top three economic powers in the world over the next 10-15 years, backed by its robust democracy and strong partnerships. Indian economy has the potential to grow at a reasonably high pace in the post-pandemic scenario. There are signs that consumption demand, triggered by festive season, is making a strong comeback. Fuel duty cuts will increase the purchasing power, which can create additional consumption. We are heading towards better times and are optimistic that the current year and beyond would be reflective of a better forecast as per global economic predictions.

Government and Regulatory Bodies continue to function seamlessly and issue and amend necessary regulations to improve compliance, clear out the confusions and aid businesses.

With an endeavour to provide insights on such newly brought in amendments and ensure compliance to safeguard the stakeholders interest, we are pleased to bring to you our issue covering the key updates announced in the month of October and the ones relevant in the current period.

SEBI, with a view of ease of doing business and protecting investor's interest, has been proactive by introducing various reforms including clarification on maintenance of current accounts by stock brokers, amendments in Corporate Governance for Debt Listed Entities, regulations in relation to the listing of entities who have issued Superior Voting Rights ("SR") equity shares, authorisation of cost accountant to issue share reconciliation capital audit report, etc.

Further, MCA has provided relief by extending the due date of filing the cost audit report under Rule 6(5) of the Companies (Cost Records and Audit) Rules, 2014.

RBI has also released master circular relating to prudential norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances. It has also released master directions for all Banks, Financial Institutions & Non-Banking Financial Companies in relation to Securitisation of Standard Assets and Master Directions in relation to transfer of loan exposure.

We aim to provide an overview of these updates in a simplified manner along with highlighting key changes and implications in order to keep you up to date with the relevant changes. We believe that our publication will be beneficial to you enabling adherence to compliances and ensuring better corporate governance.



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Maintenance of current accounts in multiple banks by Stock Brokers

The market regulator, Security Exchange Board of India (SEBI), vide its circular dated 28th October 2021 has provided clarification, to facilitate seamless settlement of funds and the convenience of investors, that the Stock Brokers should maintain current accounts in appropriate number of banks (subject to the maximum limit prescribed by Stock Exchanges/SEBI from time to time) for holding the client funds (i.e., Client Account), for settlement purposes and any other accounts mandated by Stock Exchanges such as exchange dues account subject to condition that brokers are using these accounts for their defined purposes.

Security Exchange Board of India, vide its prior Circulars, had mandated that all the brokers shall maintain separate bank accounts each for the clients' money and their own in order to ensure transparency along with guidelines on uniform nomenclature to be followed by Stock Brokers for naming and tagging of bank accounts.

RBI, vide circular no. DOR.- No.BP.BC/7/21.04.048/2020-21 dated 6th August, 2020, had instructed banks not to open current accounts for customers who have availed credit facilities in the form of cash credit (CC)/ overdraft (OD) from the banking system and all transactions to be routed through the CC/OD account itself. However, on a review, RBI on 14th December 2020, permitted banks to open specific accounts which are stipulated under various statutes and instruction of other regulators/regulatory departments, without any restrictions.

Consequent to the aforementioned circulars issued by RBI, SEBI received multiple representations regarding the problems being faced by stock brokers in maintaining current accounts in multiple banks following which SEBI vide its circular dated 28th October 2021, clarified that the Stock Brokers should maintain current accounts in appropriate number as explained above.

Nangia's Take

SEBI's clarification regarding maintaining of current accounts with multiple banks has come up as a relief to stock brokers as well as investors. The move is intended at facilitating financial inclusion, convenience of investors and stock brokers coupled with assistance in ease of doing business.

Corporate Governance for Debt Listed Entities by SEBI- a move towards transparency and promptness of information

It is an undeniable fact that debt in India is mostly privately placed which largely involves the Qualified Institutional Buyers (QIBs). Public participation is almost negligible resulting in no injustice to them at large. Keeping that in mind, the debt listed entities were treated differently from the equity listed entities and were not subject to stricter compliances. Securities And Exchange Board Of India ("SEBI") has put an end to the easy going journey of a debt listed entity by placing them at par with the equity listed entities.

On 7th September 2021, SEBI amended¹ the provisions of Non-Convertible Securities ("NCS") laid down in the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015(LODR) mandating entities that have listed non-convertible securities to disclose financial results on a quarterly basis, including assets & liabilities and cash flows.

The evolution of these amendments was brought in by the Ministry of Corporate Affairs through the amendment² issued on 19th February 2021 which changed the definition of the listed company. Public companies which have not listed their equity shares but have debt or preference shares listed will not be counted as listed entities. Similarly, private limited companies with listed debt securities will also not be considered as listed. It was always considered that SEBI would do whatever is required to protect the interest of the public. Accordingly, SEBI came out with the alternative provision to strengthen the governance of the debt-listed companies.

Provision of these amendments would apply to high-value debt listed entities ("HVDLE")³ and the threshold is to be determined on the outstanding principal as of 31st March 2021.

Most of the corporate governance requirements that are laid down under regulations 15 to 27 of Chapter IV of Securities and Exchange Board Of India (Listing Obligations And Disclosure Requirements) Regulations, 2015 which earlier used to apply to equity listed entities would now apply to debt listed entities too. SEBI has given a reasonable time to such companies to completely comply with these requirements. Effectively there is 18 months window (Up to March 2023) within which the companies need to comply with these requirements on a explained basis. If they can't comply, they need to provide an explanation and give justification. From 1st April 2023, this becomes a mandatory requirement.

SEBI, on 5th October 2021 issued the revised format⁴ for filing financial information by companies whose non-convertible securities are listed. The format for statement of cash flow on half yearly basis is to be submitted to securities exchange, debenture trustees and on the companies website. The format will be prepared under the indirect method as prescribed in accounting standard 3 or Indian accounting standard 7 mandated under sec 133 of the companies act 2013. Where the listed entity does not have corresponding cashflow statement for the half year ended September 2020, the reporting of corresponding, the column on corresponding figures will not be applicable.

For listed entities that becomes HVDLE subsequently, would be required to comply with six months of such applicability. Under the amended regulations, debt listed entities are mandated to submit audited financial results within 60 days from the end of the financial year. Another major change brought under the amended regulation is the requirement of written consent of atleast 3/4th (by value) of securities holders is to be taken before proceeding with any material modification in the structure of NCS. Earlier there was no clarity under the SEBI (Issue and Listing of Debt Securities) Regulations, 2008 with respect to appointment of debenture trustees for private placement of debts securities. Post issuance of NCS regulation, this dilemma has been eliminated.

¹ notification No. SEBI/LAD-NRO/GN/2021/47 dated 7th September 2021 issued by SEBI.

² notification No G.S.R. 123(E). dated 19th February 2021 issued by Ministry Of Corporate Affairs

³ HVDLE mean listed entities that have listed their NCS and have an outstanding value of listed NCS of `500 crore or more.

⁴ Circular no SEBI/HO/DDHS/CIR/2021/0000000637 dated 5th October 2021 issued by SEBI.

Further to these regulations, SEBI on 14th October 2021, issued a revised format⁵ for issuance of limited review report/audit report for issuers of nonconvertible securities. The formats for limited review/ audit reports on financial information to be implemented by listed entities other than insurance companies. Insurance companies would disclose limited review/ audit reports as per the formalities specified by IRDAI.

The formats for limited review/ audit reports on financial information is categorized as below:

- Limited Review Report for quarterly stand alone financial results for entities other than Banks, NBFC
- Limited Review Report for quarterly stand alone financial results for Banks and NBFCs.
- Audit Report for quarterly standalone financial results for entities other than Banks, NBFCs
- Audit Report for quarterly standalone financial results for Banks and NBFCs
- Audited Annual consolidated Financial Results for entities other than Banks, NBFCs
- Audited Annual consolidated Financial Results for Banks and NBFCs

Limited Review Report will now be conducted as per the ICAI standards on Review Engagement (SRE) 2410 on "review of interim financial information". Earlier the these were conducted as per the SRE 2400 on "Engagement to review of historical financial statements".

Nangia's Take

The status of debt listed companies had undergone a change after the amendment in the definition of listed companies which is made effective from 1st April, 2021. This led to a loose ends in the corporate governance of such debt listed companies. SEBI's move of enforcing governance through these framework seems as a measure to fill the gap. These new framework are now in sync with what is applicable to equity listed entities. These step are majorly inspired by the need for more transparency and promptness of information. The extension of chapter IV to HVDIEs is an alarm for debt listed entities which are not HVDLEs as of now.

Regulatory requirements in relation to listing of entities with Superior Voting Rights equity shares

There was an increasing debate about the need to enable issuance and listing of shares with differential voting rights, commonly known as DVRs in India (dual class shares or DCS in the international context). Such shares have rights disproportionate to their economic ownership. New technology firms typically employ asset light business model whereby the firm owns relatively fewer capital assets compared to the value of its operations. Such firms prefer equity over debt capital and raising equity on a periodic basis lead to dilution of founder/ promoter stake. In such new technology firms where the promoter/ founders are instrumental in the success of the firms, there is a need for a structure to enable them to retain decision-making powers and rights vis-à-vis other shareholders. One such possible structure is issuance of shares with superior voting rights to founders/ promoters of the company.

SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 prohibits a listed company from issuance of shares which may confer on any person superior rights as to voting or dividend vis-à-vis the rights of equity shares that are already listed. Further, SEBI (ICDR) Regulations, 2018 mandates a statement that the shares issued in an issue are pari passu with the existing shares in all respects including dividend. Apart from these, Companies (Share Capital and Debentures) Rules, 2014 [Companies (SCAD) Rules, 2014] restricts issuance of DVRs only by companies having profitability track record among other conditions. The Companies (SCAD) Rules, 2014, also provides a cap of 26% on shares with differential rights of the total post issue paid up capital.

In order to do an in depth study of introduction of dual class shares in Indian Scenario sub- group of the Primary Market Advisor Committee (PMAC) of SEBI was formed in September 2018.

Post deliberations and analysis of public comments SEBI wide Securities And Exchange Board Of India (Issue Of Capital And Disclosure Requirements) (Third Amendment) Regulations, 2019 paved the way for issue of Superior Voting Rights equity shares.

In this article we have covered current regulations prescribed by SEBI in relation to the listing of entities who have issued Superior Voting Rights ("SR") equity shares.

- SR equity shares means the equity shares of an issuer having superior voting rights compared to all other equity shares issued by that issuer.
- If an issuer has issued SR equity shares to its promoters/ founders, the said issuer shall be allowed to do an initial public offer of only ordinary shares for listing on the Main Board subject to compliance with the below provisions in addition to the other conditions of Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018
 - the issuer shall be intensive in the use of technology, information technology, intellectual property, data analytics, bio-technology or nano-technology to provide products, services or business platforms with substantial value addition.
 - the net worth of the SR shareholder, as determined by a Registered Valuer, shall not be more than rupees one thousand crore (modified vide Securities and Exchange Board of India (issue of capital and disclosure requirements) (fourth amendment) regulations, 2021 dated October 26, 2021 from the shareholder shall not be part of the promoter group whose collective net worth is more than rupees 500 crores).

Further, while determining the individual net worth of the SR shareholder, his investment/ shareholding in other listed companies shall be considered but not that of his shareholding in the issuer company.

Modified vide Securities and Exchange Board of India (issue of capital and disclosure requirements) (fourth amendment) regulations, 2021 dated October 26, 2021 from while determining the collective net worth, the investment of SR shareholder in the shares of the issuer company shall not be considered).

- The SR shares were issued only to the promoters/ founders who hold an executive position in the issuer company;
- The issue of SR equity shares had been authorized by a special resolution passed at a general meeting of the shareholders of the issuer, where the notice calling for such general meeting specifically provided for -
 - a. the size of issue of SR equity shares,
 - b. ratio of voting rights of SR equity shares vis-à-vis the ordinary shares
 - c. rights as to differential dividends, if any
 - d. sunset provisions, which provide for a time frame for the validity of such SR equity shares,
 - e. matters in respect of which the SR equity shares would have the same voting right as that of the ordinary shares,
- the SR equity shares have been issued prior to the filing of draft red herring prospectus and held for a period of at least three months prior to the filing of the red herring prospectus (modified vide Securities and Exchange Board of India (issue of capital and disclosure requirements) (fourth amendment) regulations, 2021 dated October 26, 2021.
- The SR equity shares shall have voting rights in the ratio of a minimum of 2:1 upto a maximum of 10:1 compared to ordinary shares and such ratio shall be in whole numbers only;
- The SR equity shares shall have the same face value as the ordinary shares;



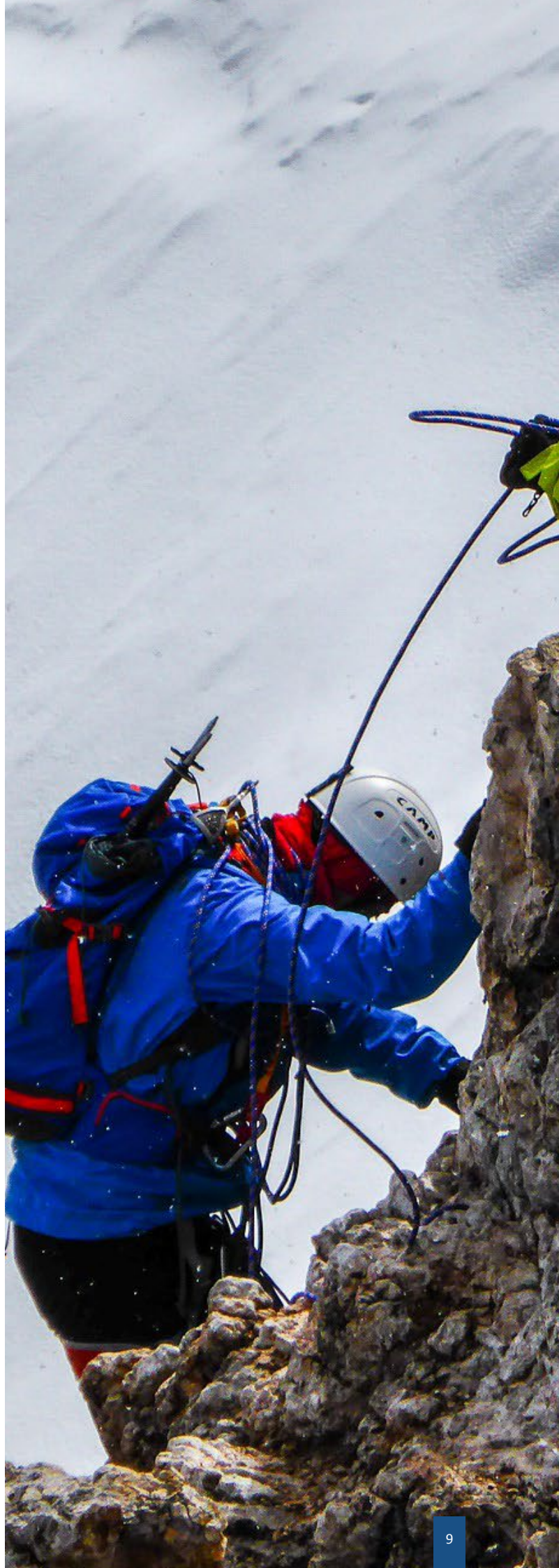
- The issuer shall only have one class of SR equity shares;
- The SR equity shares shall be equivalent to ordinary equity shares in all respects, except for having superior voting rights.
- The SR equity shares shall be under lock-in until conversion into equity shares having voting rights same as that of ordinary shares or eighteen months from the date of allotment in the initial public offer whichever is later.
- SR securities cannot be pledged as a collateral security for a loan granted by a scheduled commercial bank or a public financial institution or a systemically important non-banking finance company or a housing finance company.
- SR securities cannot be transferred to any another promoter or any person of the promoter group or a new promoter.
- Where the issuer has issued SR equity shares to its promoters or founders, then such a SR shareholder shall not renounce their rights and the SR shares received in a rights issue shall remain under lock-in until conversion into equity shares having voting rights same as that of ordinary equity shares along with existing SR equity shares.
- The SR equity shares of promoters, if any, shall be eligible towards computation of minimum promoters' contribution to be satisfied for the purpose of proposed issue of shares.
- If an issuer has issued SR equity shares to its promoters or founders, any bonus issue on the SR equity shares shall carry the same ratio of voting rights compared to ordinary shares and the SR equity shares issued in a bonus issue shall also be converted to equity shares having voting rights same as that of ordinary equity shares along with existing SR equity shares.

Nangia's Take

- SR shares gives more pliability to the founders of new-age companies for raising capital and taking their company public.
- **Net worth of SR shareholders:** Under earlier norms SR shares cannot be issued to an entity that is part of a promoter group with a collective net worth of more than Rs 500 crore this had led to a situation where the net worth of the relatives of founders was included acting as roadblock for new technology companies for listing by amendment SEBI has relaxed rules.
- **Timing of issuance of SR shares:** Under earlier norms require SR shares to have been held for at least six months prior to the filing of the initial share sale prospectus. SEBI has reduced the period to 3 months as this leads to delays in issuing shares through an IPO.

Other key amendments and directions recently issued

- Ministry of Corporate Affairs vide circular dated 29th October' 2021 has further extended due date of filing of cost audit report to the Board of Directors under Rule 6(5) of the Companies (Cost Records and Audit) Rules, 2014 by one month and is now due to be filed by 30th November' 2021. This is done in view disruptions caused by Pandemic.
- SEBI has amended the Securities and Exchange Board of India (Depositories and Participants) (Second Amendment) Regulations, 2018. Post amendment practicing cost accountants are also now authorised to issue share reconciliation capital audit report besides practicing Chartered Accountants and Company Secretaries.
- RBI has released a Master Circular dated October 1, 2021 for all Banks that consolidates instructions and guidelines to be followed by Banks on matters relating to prudential norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances.
- RBI has released with immediate effect Master Directions dated September 24, 2021 for all Banks, Financial Institutions & Non-Banking Financial Companies in relation to Securitisation of Standard Assets and Master Directions in relation to transfer of loan exposure. All lending institutions including Banks, FIs & NBFCs are required to ensure compliance with the new regulations in place of the erstwhile existing regulations.



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