KNOWLEDGEWARE
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REGULATORY

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Editorial:

Dear Esteemed Readers,

We are pleased to share with you March 2016 Regulatory Newsletter covering regulatory updates in India. Even as we write this piece the flurry of regulatory updates by the Ministry of Corporate Affairs seems to have suddenly increased with the issue on March 30, 2015 of the IND AS Accounting Amendment Rules, Accounting Standards Amendment Rules, the CARO 2016 and 2 Removal of Difficulties Orders.

The IND AS amendment rules amend 19 existing IND AS standards, include two new standards – IND AS 18 Revenue and IND AS 11 Construction Contracts to replace IND AS 115 (which had been a demand of the industry), articulating an IND AS roadmap for NBFCs, and other matters. Similarly the Accounting Standards Amendment Rules, include 7 standards to replace existing accounting standards for entities not required to adopt IND AS.

While the replacement of IND AS 115 with IND AS 18 and 11 may be welcome the other amendments to the other standards would need to be evaluated and come very close to the time by which listed companies are readying themselves to prepare their first IND AS compliant quarterly results.

Similarly the changes proposed to the existing accounting standards via the Accounting Standards Amendment Rules applicable to entities not required to apply IND AS at present will also mean extra effort for these entities while closing their books, as some of the new standards appear to be different from the existing ones. Again listed companies may be impacted.

Given the above, one wonders if the timing of the issuance could have been better and whether there should be better coordination between regulators, eg the issuance of these by MCA if combined with some relief in timeline given by SEBI could have resulted in entities having more time to apply their minds to the implications of these changes.

Similarly the SEBI has issued a revised circular on manner of dealing with qualified audit reports and now requires companies to quantify the total impact of audit qualifications in the Form B to be submitted and removes the requirement to file Form A (non qualified reports). It is a moot point as to whether this is again a duplication as the auditing standards also requires auditors to give the total effect of audit qualifications in the audit report and management to put in their responses to such qualification in the notes. While SEBI wants to move to a regime of unqualified audit reports, it is not clear how this can be done where the qualification is on a judgmental matter where the auditor’s differs from management when the auditor is not privy to the same information as management.

Among other updates the last month of this financial year has too ended with the release of a few other important updates from the Reserve Bank of India, Insurance regulator IRDAI and the capital market regulator SEBI including:

- RBI revising prudential guidelines on revitalising stressed assets
- Reserve Bank of India (RBI) issues Master Direction on Interest Rate on Advances and on Deposits
- Discussion Paper on 'Bright-line tests for acquisition of Control' under SEBI Takeover Regulations, 2011
- Roadmap by IRDAI to insurance companies on preparing IND AS financial statements

While we are seeing introduction of a lot of regulations to move towards the principle thatregulationis expected to ensure that the institutional mechanisms are functioning in the expected manner and are continuously producing trust.

Happy Reading and wishing you a very happy start of the new Fiscal year 2017!

Happy reading!

Yours Sincerely,

Knowledgeware Team

B. K. Khare & Co.

Reserve Bank of India (RBI)

Reserve Bank of India (RBI) on review of risk weights assigned to sovereign debt

Presently, (a) deposit accepting NBFCs, (b) systemically important non-deposit accepting NBFCs, (c) NBFC – MFIs and (d) NBFC – IFCs are required to maintain capital adequacy ratio consisting of Tier I and Tier II capital which is not less than 15% of its aggregate risk weighted assets on balance sheet and off balance sheet.

Based on representations received from industry, RBI has reviewed and revised the risk weights assigned to domestic sovereign exposures from the earlier 15%, as under :

		Type of Exposure	Risk Weight
A		Exposure to Central Government	
	i.	Fund based claims	0%
	ii.	Non Fund based claims guaranteed by Central Government	0%
B		Exposure to State Government	
	i.	Direct loans/ credit or overdraft exposure and investment in State Government securities	0%
	ii.	Non Fund based claims guaranteed by State Government	20%
	iii.	Loans guaranteed by State Government which are in default for more than 90 days	100%

RBI Reference : RBI/2015-16/336 dated 10th March 2016

Reserve Bank of India (RBI) issues notification on Application of Minimum Capital Adequacy Norms to State and Central Cooperative Banks (StCBs/CCBs)

StCBs and CCBs will now be permitted to also include the following items under Tier I capital from the financial year commencing from 1st April, 2015 –

i. Contributions received from associate / nominal members where the bye-laws permit allotment of shares to such members and provided there are restrictions on withdrawal of such shares as applicable to regular members.
ii. Contribution / non-refundable admission fees collected from the nominal and associate members, which are held separately as 'Reserves' under appropriate head since these are not refundable.
iii. Outstanding amount in Special Reserve created under Section 36(1) (viii) of the Income Tax Act, 1961, if the bank has created Deferred Tax Liability (DTL) on this Reserve.

This will help StCBs and CCBs to boost Tier I capital, providing strength to Capital to Risk Weighted Assets Ratio (CRAR).

RBI circular: RBI/2015-16/335 dt. March 10, 2016

Reserve Bank of India (RBI) notification for revised Framework for Revival and Rehabilitation of Micro, Small and Medium Enterprises (MSMEs)

In order to provide a simpler and faster mechanism to address the stress in the accounts of MSMEs and to facilitate the promotion and development of MSMEs, the Ministry of Micro, Small and Medium Enterprises, Government of India, vide their Gazette Notification dated May 29, 2015 had notified a 'Framework for Revival and Rehabilitation of Micro, Small and Medium Enterprises'. However, certain changes in the captioned framework have been carried out in consultation with the Government of India, Ministry of MSME in order to make it compatible with the existing regulatory guidelines on 'Income Recognition, Asset Classification and provisioning pertaining to Advances' (IRAC) issued to banks by RBI. Accordingly, the revised Framework along with operating instructions is furnished as an Annexure to this notification. The Board approved policy to operationalize the Framework may be put in place by the banks not later than June 30, 2016.

The new Framework provides for detailed guidelines on identification of incipient stress, formation of Committees for Stressed SMEs, Corrective Action Plans and several other procedures.

The revival and rehabilitation of MSMEs having loan limits up to Rs.25 crore will be in terms of these operating instructions. Restructuring of loan accounts with exposure of above Rs.25 crore will continue to be governed by the extant guidelines on Corporate Debt Restructuring (CDR) / Joint Lenders' Forum (JLF) mechanism.

The revised Framework supersedes the earlier Guidelines on Rehabilitation of Sick Micro and Small Enterprises issued on November 1, 2012, except those relating to *Reliefs and Concessions for Rehabilitation of Potentially Viable Units and One Time Settlement*, mentioned in the said circular.

This notification is directed towards all Scheduled Commercial Banks who are supposed to furnish Action Taken Report by **July 31, 2016** to RBI.

RBI Circular.: RBI/2015-16/338 FIDD.MSME & NFS.BC.No.21/06.02.31/2015-16 dated March 17, 2016

RBI aligns treatment of certain balance sheet items in computation of Tier I Capital with BCBS prescription

The banks have been representing to RBI that the treatment of certain balance sheet items, as per the existing regulations on banks' capital, differ from what is prescribed by the Basel Committee on Banking Supervision (BCBS). This places on the banks in India the need to raise more capital than would be required had the Basel rules been applied as they exist.

The Reserve Bank on review decided to align, to some extent, the current regulations on treatment of certain balance sheet items, for the purpose of regulatory capital, with the BCBS guidelines. Accordingly revision in Basel III norms for banks in India has been introduced on 1 March 2016.

The relaxation provided in respect of inclusion of certain balance sheet items in Common Equity Tier I capital ('CET1') is as follows:

Treatment of revaluation reserves

Revaluation reserves arising out of change in the carrying amount of a bank's property consequent upon its revaluation, may, at the discretion of banks, be reckoned as CET1 capital at a discount of 55%, instead of as Tier 2 capital under extant regulations, subject to meeting the following conditions:

- bank is able to sell the property readily at its own will and there is no legal impediment in selling the property;
- the revaluation reserves are shown under Schedule 2: Reserves & Surplus in the Balance Sheet of the bank;
- revaluations are realistic, in accordance with Indian Accounting Standards.
  This is subjective, difficult to pin down on 'realistic valuation'

- valuations are obtained, from two independent valuers, at least once in every 3 years; where the value of the property has been substantially impaired by any event, these are to be immediately revalued and appropriately factored into capital adequacy computations;
- the external auditors of the bank have not expressed a qualified opinion on the revaluation of the property;
- the instructions on valuation of properties and other specific requirements as mentioned in the 2007 circular on 'Valuation of Properties - Empanelment of Valuers' are strictly adhered to.

Treatment of foreign currency translation reserve (FCTR)

Banks may, at their discretion, reckon foreign currency translation reserve arising due to translation of financial statements of their foreign operations in terms of Accounting Standard (AS) 11 as CET1 capital at a discount of 25% subject to meeting the following conditions:

- the FCTR are shown under Schedule 2: Reserves & Surplus in the Balance Sheet of the bank;
- the external auditors of the bank have not expressed a qualified opinion on the FCTR.

The above may have limited relevance as AS 11 will become history in couple of years and corresponding Ind AS will become applicable.

Treatment of deferred tax assets (DTAs)

(i) Deferred tax assets (DTAs) associated with accumulated losses and other such assets should be deducted in full from CET1 capital.

(ii) DTAs which relate to timing differences (other than those related to accumulated losses) may, instead of full deduction from CET1 capital, be recognised in the CET1 capital up to 10% of a bank's CET1 capital, at the discretion of banks. Further DTAs and DTLs may be netted off against each other on proportionate basis if such netting off of tax liabilities is permissible under relevant tax law of the country

(iii) Further, the limited recognition of DTAs as at (ii) above along with limited recognition of significant investments in the common shares of unconsolidated financial (i.e. banking, financial and insurance) entities taken together must not exceed 15% of the CET1 capital,

(iv) The amount of DTAs which is not deducted from CET1 capital (in terms of para (ii) above) will be risk weighted at 250% as in the case of significant investments in common shares not deducted from bank's CET1 capital.

RBI circular RBI/2015-16/331 dated 1 March 2016

Reserve Bank of India (RBI) issues Master Direction on Interest Rate on Advances

In exercise of the powers conferred by Sections 21 & 35A of the Banking Regulation Act, 1949, the Reserve Bank of India being satisfied that it is necessary and expedient in the public interest, has issued Master Direction – Reserve Bank of India (Interest Rate on Advances) Directions, 2016.

These directions shall apply to every Schedule Commercial Bank, **excluding** Regional Rural Banks (RRBs) licensed to operate in India by RBI. The Directions are divided in seven chapters and may be summarized as below

Chapter I – Preliminary:

- The applicability of the directions, including the definitions for terms included in the guidelines

Chapter II – General Guidelines:

- Interest rate framework and directions, impetus on a duly approved comprehensive policy on interest rates on advances, terms and conditions on charge of interest for various products.
- Banks shall determine their actual lending rates on advances in all cases by adding the components of spread to the internal benchmark rate & there shall be no lending below the Base rate or MCLR (Marginal Cost of Funds based Lending Rate)
- Penal Interest: Banks shall formulate a Board approved fair and transparent policy for charging penal interest on advances.

Chapter III – Benchmark

Internal Benchmark - Base Rate:

- Banks shall have only one base rate and banks shall not review the Base Rate methodology for at-least a period of three years from the date of its finalization
- Guidelines on calculation and inclusions and review of Base Rate

Internal Benchmark – Marginal Cost of Funds based Lending Rate (MCLR):

- All rupee loans sanctioned and credit limits renewed w.e.f. April 1, 2016 shall be priced with reference to the Marginal Cost of Funds based Lending Rate (MCLR) which will be the internal Benchmark for such purposes

- The MCLR shall comprise of:
  a. Marginal Cost of Funds – Marginal cost of borrowings and return on net-worth
  b. Negative carry on account of CRR calculated as – **Required CRR * (marginal cost)/(1-CRR)**
  c. Operating Costs – Inclusions and exclusions
  d. Tenor Premium – Tenor premium to be uniform for all types of loans for a given residual tenor.
- Review of MCLR on a monthly basis.

External Benchmark – Banks shall have freedom to determine the interest rates on advances linked to market determined external benchmarks

Chapter IV – Interest Rates on Advances

- Spread: The banks shall have a Board approved policy delineating the components of spread charged to customer
- Spread guidelines under Base Rate System
- Spread under MCLR system, its components viz., Business strategy & Credit risk premium
- Guidelines for reset of interest masters under MCLR which shall be done by banks at their option,
- MCLR prevailing on the day of the loan shall be applicable till the next reset date, irrespective of changes in the benchmark during the interim
- Transition to Base rate from BPLR: Existing loans based on BPLR shall run till their maturity and the borrowers desirous of switching to new Base Rate system, shall be given an option on mutually agreed terms with further charge of fees for such switch-over
- Transition to MCLR from Base Rate: Existing loans shall continue till repayment/renewal and borrowers shall have the option to move to MCLR and the switch-over shall not be treated as a foreclosure of an existing facility

Chapter V – Foreign Currency Advances

- Guidelines on interest rates on advances in foreign currency

Chapter VI –Exemptions

- Exemptions from the guidelines

Chapter VII – Repeal & other provision

- List of circulars issued by the RBI which stand repealed with the issue of these directions

The revision in the benchmarking system will have a considerable impact on the Indian Banking system and consequently on the India economy as a whole. The move further consolidates the regulator's commitment towards transparency in the loan system.

RBI circular reference: RBI/DBR/2015-16/20 Master Direction DBR.Dir.No.85/13.03.00/2015-16

Reserve Bank of India (RBI) issues Master Direction on Interest Rate on deposits

In exercise of the powers conferred by Sections 21 & 35A of the Banking Regulation Act, 1949, the Reserve Bank of India being satisfied that it is necessary and expedient in the public interest, has issued Master Direction – Reserve Bank of India (Interest Rate on Deposits) Directions, 2016.

These directions shall apply to every Schedule Commercial Bank, including Regional Rural Banks (RRBs) licensed to operate in India by RBI. The Directions are divided in seven chapters and may be summarized as below

Chapter I – Preliminary:

- The applicability of the directions, including the definitions for terms included in the directions

Chapter II – General Guidelines:

- Interest rate framework and directions, terms and conditions for payment of interest on deposits of money (other than current account deposits).
- For deposits maturing for payment on non-business working day, the interest to be paid for the non-business working day
- Consequence of transfer of deposit account from one bank branch to the other bank branch whereby, the deposit will continue to be governed by the terms of contract and the same rate of interest as agreed to between the customer and the bank branch being taken over

Chapter III – Domestic Rupee Deposits

- Guidelines on interest rates on Domestic Rupee Deposits, including Savings deposits, Current Deposits, Term Deposits, additional interest on domestic deposits, interest on overdue domestic deposits & interest payable on domestic deposit account of the deceased depositor
- Periodicity of payment of interest on domestic savings deposits
- Penalty on premature withdrawal of domestic term deposits whereby, banks shall have comprehensive policy on penalties with clarity of components of penalty to be clearly brought to the notice of the depositors at the time of acceptance

Chapter IV – Rupee Deposits of Non-Residents

- Guidelines on interest rates on non-resident deposits including interest payable on the NRE term deposit account of deceased depositor
- Penalty on premature withdrawal of domestic term deposits whereby, banks shall have comprehensive policy on penalties with clarity of components of penalty to be clearly brought to the notice of the depositors at the time of acceptance

Chapter V – Foreign Currency Deposits

- Guidelines on interest rates on Foreign Currency (Non Residents) accounts (FCNR) and the manner of calculation of interest on FCNR (B) accounts
- Guidelines on interest payable on deposit of deceased FCNR (B) depositor, payment of interest on FCNR (B) deposits of NRIs returning to India, and, conversion of FCNR (B) of returning Indians into RFC/Resident Rupee accounts
- Penalty on premature withdrawal of domestic term deposits whereby, banks shall have comprehensive policy on penalties with clarity of components of penalty to be clearly brought to the notice of the depositors at the time of acceptance
- Scheduled Commercial Banks shall have freedom to determine interest on deposits accepted/renewed under the RFC account scheme as per the comprehensive policy on interest rates on deposits as duly approved by the BOD or any committee of the Board to which powers have been delegated.

Chapter VI – Prohibitions and Exemptions

- Prohibitions imposed to comply with the ethical business practices
- Exemptions from the guidelines

Chapter VII – Repeal & other provision

- List of circulars issued by the RBI which stand repealed with the issue of these directions

The detailed nature of the directions is a welcome step in the current dynamic banking scenario and should help to boost depositor/customer confidence for transparency expected from the banks.

RBI circular reference:RBI/DBR/2015-16/19 Master Direction DBR. Dir. No.84/13.03.00/2015-16

Grant of EDF Waiver for Export of Goods Free of Cost

GOI vide amendment notification No. 9/2015-2020 dated June 4, 2015, has notified that Status Holders are now entitled to export freely exportable items on free of cost basis for export promotion subject to an annual limit of Rs 10 lakh or 2% of average annual export realization during preceding three licensing years whichever is lower.

In such cases, AD Category – I banks can consider the requests from Status Holder exporters towards waiver of Export Declaration Form (EDF) for export of goods free of cost based on the revised norm.

Circular No: RBI/2015-16/332 A.P. (DIR Series) Circular No.53 dated 03 March, 2016

RBI revises prudential guidelines on revitalising stressed assets

The Reserve Bank of India (RBI), through its notification dated 25 February 2016, issued certain revisions and clarifications to its prudential guidelines on Strategic Debt Restructuring (SDR) and on the Framework to revitalise the distressed assets through Joint Lenders' Forum Empowered Group (JLF-EG). It re-emphasises the requirement for banks to stringently adhere to previously-issued guidelines including those relating to triggers for invoking SDR, effecting a change in the management of borrower companies, invoking personal guarantees obtained from existing promoters and conversion of debt into equity shares of the borrower within the specified timeframe.

The current notification prospectively modifies some of the previously-issued guidelines on SDR. Significant modifications are:

Minimum equity divestment to obtain asset classification benefit

- Minimum quantum of equity to be divested by banks within 18 months to new promoters, in order to retain the benefit relating to the classification of the asset as 'standard', has been revised to 26 per cent from 51 per cent previously.
- Lending banks will have the option of exiting their remaining holdings gradually, with an upside as the company turns around. Timelines for conversion of debt into equity have been specified.

Timelines for conversion of debt into equity

- Joint Lenders Forums (JLFs) are required to adhere to the prescribed timelines during the SDR process, the notification permits flexibility in the completion of individual activities up to the conversion of debt into equity in favour of the lenders. However, it requires such conversions to be completed within a period of 210 days from the date a decision to invoke SDR is made (based on a review of the achievement of milestones/critical conditions by the borrower).
- If this timeline is not met with, the benefit of a 'standstill' in the asset classification which was available from the date the SDR was invoked (the reference date) ceases to exist. The loans will then be classified in accordance with the existing 'Income Recognition, Asset Classification (IRAC) and Provisioning Norms' prescribed in the RBI's Master Circular dated 1 July 2015.

Additional provisioning requirements

- Previously-issued guidelines on the SDR scheme, as defined in the RBI Circular dated 8 June 2015, exempted banks from the requirement of a periodic mark-to-market of the equity shares of the borrower received on the conversion of debt, for the 18 month period until divestment to the new promoters. The notification now requires banks to periodically value and provide for depreciation on these equity shares as per IRAC norms for investments. However, banks have the option of distributing the depreciation in value, if any, over a maximum of four calendar quarters from the date of conversion of debt into equity
- In addition, banks are required to ensure that they hold a provision of at least 15 per cent of the residual loan by the end of 18 months from the reference date. This is to avoid a sharp

deterioration in the asset classification if the banks are unable to divest a minimum equity stake to new promoters within the stipulated 18 month period. This provision is also to be made in equal instalments over four quarters and can be reversed only when all the outstanding facilities in the account perform satisfactorily after the transfer of ownership and management control to the new promoters.

Change in prudential guidelines on restructuring of advances

- As per para 17.1.5 of Master Circular on IRAC Norms dated July 1, 2015 the borrowers indulging in frauds and malfeasance will continue to remain ineligible for restructuring. On a review, it has been decided that in cases of fraud/malfeasance where the existing promoters are replaced by new promoters and the borrower company is totally delinked from such erstwhile promoters/management, banks and JLF may take a view on restructuring of such accounts based on their viability, without prejudice to the continuance of criminal action against the erstwhile promoters/management

Key changes to JLF-EG guidelines:

Streamlining the approval and JLF-EG composition process:

- In terms of paragraph 3.2 of the circular on revitalizing distressed assets dated September 24, 2015, JLF will finalise the Corrective Action Plan (CAP) and the same will be placed before an Empowered Group (EG) of lenders, which will be tasked to approve the rectification/restructuring packages under CAPs. In terms of the extant guidelines, the decisions on the CAP must be approved by a minimum of 75% of creditors by value and 60% of creditors by number in the JLF. On a review, the proportion of lenders, by number, required for approving the CAP has been reduced to 50%.
- JLF-EG composition stands modified basis the composition of lenders and the permanent member banks such as ICICI and SBI

With March 16 year-end in sight and the position of stressed accounts (including potential delinquencies) especially in case of PSU banks continuing to remain in strain, banks should carefully assess the procedural changes as well as the additional provisioning requirements, which are expected to have a significant impact on banks' financial statements in the next financial year. Nevertheless, a focused effort on the part of RBI to tackle its long-standing and most sensitive issue of the banking system and also to update/revisit the regulations basis the feedbacks received from industry, various stakeholders deserves an applaud.

RBI circular reference: RBI/2015-16/330 DBR.BP.BC.No.82/ 21.04.132 / 2015-16

Securities and Exchange Board of India (SEBI)

SEBI Board meeting: unveiling the revised procedure for dealing with qualified audit reports

SEBI has put in place a mechanism to review the audit qualifications contained in the audit reports. The said mechanism has been incorporated in the SEBI (Listing and Other Disclosure Requirements) Regulations, 2015 ('Listing Regulations'). The Regulation 33(4) of the same deals with Applicable formats of financial results, Form A (for an audit report with an unmodified opinion), and Form B (for an audit report with a modified opinion). Schedule VIII of the Listing Regulations lays down the manner of reviewing Form B accompanying the annual audited results.

With the objective that the impact of the audit qualification is disseminated without any delay and to further streamline the process the Board approved the following revised procedure to deal with such matters:, SEBI through its Board meeting held on 12 March 2016 and a press release - PR No. 56/2016, approved a revised mechanism to 'review the audit qualifications contained in the audit reports.

Revised procedure would be:

1. Listed entities shall be required to disclose the cumulative impact of all the audit qualifications on relevant financial items in a separate form called 'Statement on Impact of Audit Qualifications' instead of the present Form B. Such disclosure would be in a tabular form along with the annual audited financial results filed in terms of the Listing Regulations.
2. In cases where there are no audit qualifications, the existing requirement of filing Form A signed by top officials/directors of the company and auditors shall not be necessary.
3. The management shall have the right to give its views on the audit qualifications in the new form.
4. The existing requirement of adjustment in the books of accounts (as per Schedule VIII of the Listing Regulations) of the subsequent year shall not be necessary.

The new mechanism would be applicable from the financial year ended 31 March 2016, as well as for the earlier cases. This is a welcome change as, in line with its objectives, SEBI has continually striven to enhance the quality of financial reporting by listed companies. The financial impact of audit qualifications on financial statements would serve to be useful information for the stakeholders.

However, a detailed guidance/circular is expected from SEBI in this regard so as to clarify whether the procedure laid down in Schedule VIII of the Listing Regulations might still be required to be followed.

Assuming Schedule VIII procedure is not required to be followed going forward, then this would be a significant change as it would help to shorten the audit qualifications review process. Also, it seems, companies may not be required to:

- submit revised pro-forma financial results incorporating the effect of the modified opinion, to the stock exchanges, and
- present the accounting impact of the modified opinion as a prior period item in the financial statements of the subsequent year.

SEBI press release: SEBI Board meeting, PR no. 56/2016

Securities and Exchange Board of India (SEBI) circular for inclusion of Commodity derivatives in Securities and Exchange Board of India (International Financial Services Centres) Guidelines, 2015 (IFSC Guidelines)

SEBI (International Financial Services Centers) Guidelines, 2015 were issued on March 27, 2015 to facilitate and regulate financial services relating to securities market in an International Financial Services Centre set up under Section 18(1) of Special Economic Zones Act, 2005 and matters connected therewith or incidental thereto.

Pursuant to Section 131 of the Finance Act, 2015 and Central Government notification S.O. 2362 (E) dated August 28, 2015, all recognized associations (commodity derivatives exchanges) under the Forward Contracts (Regulation) Act, 1952 (‘FCRA’) are deemed to be recognized stock exchanges under the Securities Contracts (Regulation) Act, 1956 (‘SCRA’). Section 133 of the Finance Act, 2015 had amended Securities Contracts (Regulation) Act, 1956 to include "Commodity Derivatives" as securities.

Sub-clause (vi) of Clause 7 of IFSC Guidelines, 2015 provides that "Such other securities as may be specified by the Board". Accordingly, it is now specified that the "Commodity Derivatives" shall be eligible as securities for trading and the stock exchanges operating in IFSC may permit dealing in Commodity Derivatives.

This is a welcome inclusion considering the current trend in financial markets of exploring more opportunities in commodity markets.

SEBI Circular no.: CIR/MRD/DSA/41/2016 dated March 17, 2016

SEBI issues a Discussion Paper on 'Bright-line tests for acquisition of Control' under SEBI Takeover Regulations, 2011: Public comments sought on the options provided

The Takeover Regulations prescribe that an acquirer acquiring substantial shares or voting rights i.e., 25% or more, has to make an open offer to the public shareholders of the target company. Irrespective of the shares or voting rights acquired, the acquirer also has to make an open offer upon acquiring control of the target company. Also, Regulation 2(e) of the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 (SEBI Takeover Regulations, 2011)

defines '*control*' as *"the right to appoint majority of the directors or to control the management or policy decisions exercisable by a person or persons acting individually or in concert, directly or indirectly, including by virtue of their shareholding or management rights or shareholders agreements or voting agreements or in any other manner provided that a director or officer of a target company shall not be considered to be in control over such target company, merely by virtue of holding such position"*

The definition is more a principle-based definition rather than a rule-based. The assessment of control requires a consideration of the facts and circumstances of each case.

Similarly, the word *Control* is also defined under other laws in India such as the Companies Act, 2013, Insurance Laws (Amendment) Act, 2015, Consolidated Foreign Direct Investment (FDI) Policy Circular of 2015.

The SEBI has in the past received representations from various stakeholders to seek guidance on the definition of control and to define 'bright-lines' while assessing the various factors leading to control. Accordingly, SEBI issued a Discussion Paper ('the Paper') on 14 March 2016 seeking comments from the general public before 14 April 2016 on its proposals defining the bright-line tests for the acquisition of control under the SEBI Takeover Regulations, 2011.

After deliberating the 'wording nuances' or 'substance requirements' of a '*Control*' definition as defined under various Indian laws and regulations, the international position, and therefore the need for bright-line tests, the Paper lists down two options to determine 'control' viz.

1. **Option 1 - Framework for protective rights:**

    (a) Veto rights not amounting to the acquisition of control may be protective in nature rather than participative i.e. such rights may provide the investor **the ability to protect their investments or prevent dilution of their shareholding**. At the same time, the investor should not have the power to exercise control over the day-to-day running of the business or the policy making process. Rights over decisions involving a significant change in the current business activity or that apply in exceptional circumstances would also be treated as protective rights.

    An illustrative list of protective rights which would not amount to the acquisition of control could be:

    - Appointment of the chairman, vice-chairman, observer provided such individuals do not carry any casting vote or other voting rights.

- Rights conferred under commercial agreements provided mutual commercial benefit flows from both the sides i.e. not one-sided, the board of the target company approves the decision to enter into such an agreement, has the right to terminate the agreement, and enter into similar agreements with any other party.
- Veto rights/affirmative rights that are not part of the ordinary course of business or involve governance issues would be considered as protective in nature and would not amount to the exercise of control over the target company.
- Quorum rights i.e. for meetings involving the matters of veto rights/affirmative rights. If two meetings are not quorate, the next meeting would be deemed to have quorum despite the absence of the investor nominees.

Under this framework, the Paper specifies three conditions to be fulfilled before the above rights can be given:

- Minimum investment of 10 per cent or more in the target company.
- Grant of the protective rights would be subject to obtaining the public shareholders' approval (majority of minority). Such rights would also be required to be incorporated in the Articles of Association of a company after obtaining shareholders' approval.
- In case of initial public offers, the existing agreements would need to be cancelled/modified or suspended till the approval of public shareholders (majority of minority) is taken post-listing of the shares.

2. **Option 2 - Adopting a numerical threshold:** Under this approach,the definition of control would be amended such that control is defined as:

   a) The right or entitlement to exercise at least 25 per cent of voting rights of a company irrespective of whether such holding gives de facto control and/or

   b) The right to appoint majority of the non-independent directors of a company.

Pros and Cons of both the options are highlighted in the Paper

- **Option 1:** Although protective rights would continue to be a public shareholder and the acquisition of these rights would not amount to an acquisition of 'control' under SEBI Takeover Regulations, 2011, the acquisition of other rights would need to be examined on the basis of the facts and circumstances of each case to assess if definition of control has been met. In case such rights are deemed to be participative in nature, it would amount to 'control' and necessitate an open offer under SEBI Takeover Regulations, 2011. However, this approach may lead to further complexities in assessment of control and lead to further ambiguity in the interpretation of the definition of control.
- **Option 2-** Being a numerical threshold, it would reduce the uncertainty in the assessment of the acquisition of 'control' and provide clarity. However, in case option 2 is adopted, the acquisition of control through other means such as special rights, etc. would not necessitate an open offer requirement under SEBI Takeover Regulations, 2011 which in substance could have been participative in nature.

The DP has outlined 14 April 2016 as the last day for receiving public comments. Email id is: control@sebi.gov.in.

The issuance of this paper is a welcome step taken by the regulator by not only seeking an opinion on the proposed amendment/decision already taken on this critical subject but also providing stakeholders an opportunity to participate in the decision making process.

Subject to reading of the fine prints under various laws, positions considered under landmark judgments, stakeholders' views, following points should be considered for providing one's views:

- In substance, an assessment of control ultimately depends upon the facts and circumstances of each case.
- Many of the listed companies in India will adopt Ind AS standards from 1 April 2016. Position of Ind AS 110, *Consolidated Financial Statements* and Ind AS 103, *Business Combinations* provide a definition of control and explain when rights would be considered as protective rights. Hence, the SEBI should take into account the guidance given in Ind AS. In any case, basic premise of IFRS/Ind AS standards is principle based (therefore, the decision could be in favor of option 1)

Introduction of Exchange Traded cross currency derivatives contracts and Exchange Traded Option contracts

RBI vide A.P. (DIR Series) circular no. 35 dated December 10, 2015 has permitted recognised stock exchanges to offer cross-currency futures and option contracts in the EUR-USD, GBP-USD and USD-JPY currency pairs. RBI has also permitted recognised stock exchanges to offer currency option contracts in EUR-INR, GBP-INR and JPY-INR currency pairs, in addition to the existing USD-INR pair.

- The recognized stock exchanges have now been permitted to introduce Cross-currency futures & options contracts on EUR-USD, GBP-USD and USD-JPY and currency options on EUR-INR, GBP-INR and JPY-INR currency pairs.
- The details in terms of product design, margins and position limits for the specified currency pairs have also been defined vide the said circular.
- The existing limits of USD 15 million for USD-INR contracts and USD 5 million for non USD-INR contracts, all put together, per exchange, without having to establish underlying exposure, as laid down in SEBI circular CIR/MRD/DP/04/2015 dated April 08, 2015, have remain unchanged.
- The hedging procedure for eligible market participants as per SEBI circulars CIR/MRD/DP/20/2014 dated June 20, 2014 and CIR/MRD/DP/04/2015 dated April 08, 2015 have remain unchanged.

- Eligible market participants shall also ensure that any synthetic positions created using USD-INR, EUR-INR, GBP-INR or JPY-INR exchange traded currency derivatives contracts and exchange traded cross-currency derivatives contracts is within the position limits prescribed in SEBI circulars CIR/MRD/DP/20/2014 dated June 20, 2014 and CIR/MRD/DP/30/2014 dated October 22, 2014 for the USD-INR, EUR-INR, GBP-INR or JPY-INR derivatives contracts.
- Stock exchanges are now permitted to set trading hours for cross-currency derivatives contracts between 09:00 a.m. and 07:30 p.m.

- Stock exchanges are required to implement a mechanism of Dynamic Price Bands in the currency derivatives segment as mentioned below to prevent acceptance of orders placed beyond the price limits set by the stock exchanges:

  - Daily Dynamic Price bands for Currency futures contracts (including cross-currency):

Tenor of Contracts	Spread over theoretical price / Previous day closing price, as applicable
Up to 6 months	± 3%
> 6 months	± 5%

  The dynamic price bands shall be relaxed in increments of 1% as and when a market-wide trend is observed.

  - Dynamic Price bands for currency options contracts (including cross-currency) should be implemented based on theoretical price of contracts. The dynamic price bands can be relaxed based on market wide trend being observed in situations of high volatility.

  - Stock exchanges will have to frame suitable rules with mutual consultation for relaxation of such dynamic price bands and make it known to the market.

- The stock exchange / clearing corporation before the launch of such products will have to take an approval from SEBI giving details of contract specifications, risk management framework, surveillance systems compliance vis-à-vis the requirements specified in this circular, etc.

Circular No. SEBI/HO/MRD/DP/CIR/P/2016/0000000038 dated 09 March, 2016

Ministry of Company Affairs (MCA)

MCA releases Companies (Share Capital and Debentures) Amendment Rules, 2016

Ministry of Corporate Affairs had issued Companies (Share Capital and Debentures) Rules, 2014 on 31st March 2014 as amended by amendment rules 2014, amendment rules 2015 and second amendment rules 2015 and third amendment rules 2015.

Ministry of Corporate Affairs released the Companies (Share Capital and Debentures) Amendment Rules, 2016 on 10th March 2016 to amend clause n(iii) of Rule 17(1) of the Companies (Share Capital and Debentures) Rules, 2014.

Rule 17 basically prescribes the conditions to be complied for buy-back of shares or other securities under Section 68 of Companies Act, 2013- Power of Company to Purchase its own shares.

Applicability of Rule 17:

1. Private companies and
2. Unlisted public companies

Provision:

- Rule 17(1) provides that an explanatory statement containing various disclosures is to be annexed to the notice of general meeting. One of the disclosure is a report by company's auditors stating that calculation with reference to buy-back is done on the basis of audited accounts which are not more than six months old from the date of offer document.

Now a new proviso has been inserted to Clause n(iii) of Rule 17(1):

- Buyback calculations shall be on the basis of un- audited accounts not older than six months from the date of offer document.

- Where the audited accounts are more than six months old they shall be subjected to limited review by the auditors of the company.

The above amendment rules shall come into force from the date of publication in the Official Gazette.

Notification Ref: F. No. 01/04/2013 CL-V (Part-II) dated 10th March 2016

Ministry of Corporate Affairs (MCA) notifies Companies (Auditor's Report) Order, 2016 for the financial years commencing from April 1, 2015

The Ministry had set-up a Committee on 16 September 2015 to examine and recommend matter for inclusion in the statement to be attached with Auditor's Report under Section 143(11) of the Companies Act, 2013 for the financial year 2015-16 onwards.

The draft Companies (Auditor's Report) Order, 2016 was been placed on the MCA website. Suggestions/comments were invited latest by 23 February 2016. MCA, on 29March 2016, has notified the revised CARO w.e.f. financial year commencing on or after April 1, 2015.

It appears that, the key insertions which were proposed in the draft have been retained including:

1. Clause i(c): To confirm whether the title deeds of Immovable properties are held in the name of the company. If not, provide details.
2. Clause iv: In respect of loans, investments and guarantees, whether provisions of Section 185 and 186 of the Companies Act, 2013 have been complied with.
3. Clause xi: Whether managerial remuneration has been paid / provided in accordance with the requisite approvals mandated by the provisions of section 197 read with schedule V to the Companies Act, 2013? If not, state the amount involved and steps taken by the company for securing refund of the same.
4. Clause xiii: Whether all transactions with the related parties are in compliance with Section 188 and 177 of Companies Act, 2013 where applicable and the details have been disclosed in the Financial Statements etc as required by the accounting standards and Companies Act, 2013.
5. Clause xv: Whether the company has entered into any non-cash transactions with directors or persons connected with him and if so, whether provisions of Section 192 of Companies Act, 2013 have been complied with.

Moreover, they have added a new clause i.e. Clause xvi as to whether the Company is required to be registered under section 45-IA of the Reserve Bank of India, 1934 and if so, whether the registration has been obtained.

Proposed inclusions will eventually increase the responsibilities of an auditor significantly especially with respect to compliance of sections 185, 186 and also 188 of the Act which deal with 'related party' transactions. Since this is also covered in secretarial audit by Company Secretary, it will be duplication and possibly two different views on the same item.

Insurance Regulatory Development Authority of India (IRDA)

Insurance Regulatory Development Authority of India (IRDA) issues directions to insurers on Ind AS implementation

The Ministry of Corporate Affairs (MCA) notified the Ind AS road map for corporates on 16 February 2015. The Insurance Regulatory and Development Authority of India (IRDAI), through its order on 17 November 2015 stated that the insurance sector in India would be converging with International Financial Reporting Standards (IFRS) and subsequently on 7 December 2015, IRDAI had also issued a discussion paper on Ind AS implementation in the insurance sector with key recommendations. Further, MCA also issued a press release on 18 January 2016 outlining the road map for implementation of Ind AS in the financial services sector, including insurance companies. The IRDAI circular issued on 1 March 2016 now provides certainty on the mandate for implementation of Ind AS for all insurers.

1. Insurance companies shall comply with the Indian Accounting Standards (Ind AS) for financial statements for accounting periods beginning from April 1, 2018 onwards, with comparatives for the periods ending March 31, 2018 or thereafter. Ind AS shall be applicable to both standalone financial statements and consolidated financial statements. "Comparatives" shall mean comparative figures for the preceding accounting period. Also, no earlier adoption of Ind AS is permitted.
2. Ind AS implementation is likely to significantly impact the financial reporting systems and processes and requires fair amount of investment of time and resources in planning, management and execution. Therefore, insurers are advised to set up a Steering Committee headed by an official of the rank of an Executive Director (or equivalent) comprising members from cross-functional areas of the insurance company to immediately initiate the implementation process.
3. The Audit Committee of the Board shall oversee the progress of the Ind AS implementation process and report to the Board at quarterly intervals.
4. Focus required on certain critical implementation issues such as:
    a. Ind AS Technical Requirements: Diagnostic analysis of differences between the current accounting framework and Ind AS, significant accounting policy decisions impacting financials, drafting accounting policies, preparation of disclosures, documentation, preparation of proforma Ind AS financial statements, timing the changeover to Ind AS, and dry-run of accounting systems and end-to-end reporting process before the actual conversion.
    b. Systems and processes: Evaluate system changes - assessment of processes requiring changes, issues having significant impact on information systems (including IT systems), and develop/strengthen data capture system, where required
    c. Business Impact: Profit planning and budgeting, taxation, capital planning, and impact on capital adequacy.
    d. People - Evaluation of resources: Adequate and fully dedicated internal staff for implementation, comprehensive training strategy and program.
    e. Project management: Managing the entire process-holistic approach to planning and execution by ensuring that all linkages are established between accounting, systems, people and business, besides effective communication strategies to stakeholders.

5. Insurers shall assess the impact of the Ind AS implementation on their financial position including the adequacy of capital, taking into account the solvency regulations requirements and place quarterly progress reports to their Boards. Insurers also need to be in preparedness to submit proforma Ind AS financial statements to the Authority from the quarter ended December 31,2016, onwards.
6. Insurance companies shall disclose in the Annual Report, the strategy for Ind AS implementation, including the progress made in this regard. These disclosures shall be made from the financial year 2015-16 until implementation.

On the whole, such proactive and detailed approach spelt out by the Insurance regulator, fairly well in advance, is welcome considering the likely impact on the insurnace sector and on Indian economy as a whole.

IRDAI circular: IRDA/ F&A/CIR/IFRS/038/03/2016 dated 1 March 2016

Insurance Regulatory Development Authority (IRDA) issues circular on offering existing General Insurance Products in compliance with Micro Insurance Regulations (MIR), 2015 as General Micro Insurance Products

The Insurance Regulatory Development Authority (IRDA) has invited reference to Regulation 8(1) of MIR, 2015 which specifies that every insurer is mandated to follow the File and Use Procedure with respect to filing of Micro Insurance Products with Authority. Further reference is also invited to Schedule 1 of MIR, 2015 that specifies the terms in respect of General Micro Insurance Products defined at Regulation (2) (d) of MIR, 2015.

Authority vide Circular Ref No IRDA/Life/ Cir/ MIN/007/ 01/ 2016 dated 8th January 2016 has specified procedures for adopting the existing Micro Insurance Products so as to meet terms specified in Schedule -1 of MIR, 2015.

Insurers are permitted to adopt the existing General Insurance Products that meet the terms specified in Schedule -1 of MIR, 2015 as Micro Insurance Products by complying with the following conditions:-

1. Insurers at their discretion may offer the existing General Insurance Products that comply with product parameters specified in Schedule -1 of MIR, 2015 as General Micro Insurance Products.
2. Where the existing General Insurance Products comply with product parameters specified in Schedule -1 of MIR, 2015, on basis of a certificate to that effect filed by Appointed Actuary & CEO in prescribed format, the insurers are permitted to offer such existing General Insurance Products as General Micro Insurance Products by allotting a different product name prominently carrying a caption “Micro Insurance Product” in accordance with Regulation (8) (2) of MIR, 2015
3. The Authority on recording the proposal of Insurers may allow the Insurers to offer existing General Insurance Products as General Micro Insurance Products by allotting a Unique Identification Number (UIN)

4. On examining the product proposal submitted in accordance with this Circular, the Authority reserves the right to direct the Insurer to file the product afresh in accordance with provisions of MIR, 2015
5. There shall be no changes of any nature to existing General Insurance Products. Where any changes are necessitated in order to offer the product as General Micro Insurance Products, such products shall be separately filed in accordance with provisions of MIR, 2015

IRDA circular: IRDA/LIFE/CIR/MIN/045/03/2016dated March09, 2016

Insurance Regulatory Development Authority (IRDA) issues revised guidelines onTrade Credit Insurance

The Authority had issued guidelines on trade credit insurance on 13th December 2010 vide Circular ref IRDA/NL/CIR/CRE/205/12/2010 to regulate the business of Credit Insurance in India. In recent times the changes in economy especially in micro, small, medium enterprise sector have increased the need for trade credit and enhanced the scope for credit insurance sector manifold.

The Authority has issued revised guidelines on Trade Credit Insurance under Section 14 of IRDA Act, 1999. These guidelines come into force with immediate effect

Key features of the revised guidelines are:

1. Clause II: Applicability of “Guidelines on Product Filing Procedures for General Insurance Products” to trade credit insurance
2. Clause III: Basic Requirements of a Trade Credit Insurance Policy.
3. Clause IV: Conditions on Trade Credit Insurance applicable to Insurer and Policyholder.
4. Clause V: Trade Credit Insurance Underwriting.
5. Clause VI: Risk Management for Trade Credit Insurance.
6. Clause VII: Claims handling process of Insurer.
7. Clause VIII: Reinsurance Arrangements of Insurer
8. Clause IX: Experience and Training Requirements for employees dealing with trade credit insurance
9. Clause X: Reporting requirements to IRDAI

Revised guidelines are intended to give a fillip to growth of credit insurance market in India.

IRDA circular: IRDAI/NL/CIR/CRE/044/03/2016dated March10, 2016