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December 9, 2011 New Delhi, India

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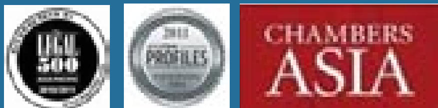
Stringent Disclosures by Domestic Indian Companies with Minority Foreign Investments

LexCounsel, Law Offices

C-10, Gulmohar Park
New Delhi 110 049, INDIA.

Tel.:+91.11.4166.2861
Fax:+91.11.4166.2862

Recommended by:



IRDA Notifies the Issuance of Capital by Life Insurance Companies Regulations, 2011

The Insurance Regulatory and Development Authority ("**IRDA**") on December 1, 2011 notified the IRDA (Issuance of Capital by Life Insurance Companies) Regulations, 2011 (the "**Regulations**") for life insurance companies/firms to raise capital from the capital market via public offerings. The Regulations have been formulated in consultation with the Securities and Exchange Board of India ("**SEBI**").

It would appear that the Regulations were implemented to give effect to section 6AA of the Insurance Act, 1938 ("**Insurance Act**") which requires promoters of Indian life insurance companies, holding more than 26% (twenty six percent) to divest the share capital in excess of 26% (twenty six percent), in a phased manner after a period of 10 (ten) years from the date of commencement of the business.

In terms of the Regulations, promoters may divest their excess shareholding through a public offer for sale under the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009 ("**ICDR Regulations**") and/or raise funds under the ICDR Regulations. However, no life insurance company can approach SEBI to undertake a public offering of its shares under the ICDR Regulations without the specific prior written approval of IRDA.

For obtaining IRDA's approval for public issue of shares, the applicant company should have completed 10 (ten) years from the date of commencement of business, which is also the time limit prescribed under section 6AA of the Insurance Act, as aforesaid. The Regulations also prescribe that life insurance companies can only issue and allot fully paid up equity shares.

While granting its approval, IRDA may impose certain conditions on the applicant company and may, inter alia, prescribe:

- the extent to which the promoters shall dilute their respective shareholding;
- the maximum subscription which could be allotted to any class of foreign investors;
- minimum lock-in period for the promoters from the date of allotment of shares. The lock-in period shall be without prejudice to the requirements which may be in place under the ICDR Regulations; and
- the disclosures in the prospectus/offer document in addition to the disclosures as may be prescribed by SEBI.

The Regulations, however, do not prescribe any time period within which the IRDA will process an application and grant approval to the applicant company for issue of capital under the ICDR Regulations. For public offerings where timelines are always a consideration, this is a let-down in view of constantly changing market conditions. Applicants would therefore need to factor in the time taken by the IRDA for grant of approval while considering a public offering. In addition, the Regulations cover initial public offerings and secondary issues. Industry analysts feel the Regulations need not cover secondary issues if the company is in continuing compliance with IRDA and SEBI regulations.

The IRDA's approval is valid for a period of 1 (one) year from the date of issue within which the applicant company should file its Draft Red Herring Prospectus with SEBI, in accordance with and as per the ICDR Regulations.

Stringent Disclosures by Domestic Indian Companies with Minority Foreign Investments

The Ministry of Finance and the Ministry of Commerce and Industry of the Government of India intend to prescribe additional disclosures by Indian companies with minority foreign ownership as regards their downstream investments in India.

In terms of the current Foreign Direct Investment Policy of India ("**FDI Policy**"), investments by an Indian company in other Indian companies is not considered as foreign investment so long as the investing Indian company is "owned and controlled" by resident Indian citizens and/or other Indian companies which are, in turn, owned and controlled by resident Indian citizens.

This exemption has led to doubts and debate that it permits foreign investments to seep into regulated and sensitive sectors of economy, such a defence, retail, etc., without Government's knowledge.

To address the above concern, the Government intends to prescribe comprehensive disclosures by Indian companies, with minority foreign investment, of investments in their subsidiary/ies. Furthermore, foreign minority shareholders of such Indian companies may also be asked to undertake, under the provisions of the Prevention of Money Laundering Act, 2002, ("**PML Act**") that they would not conduct any activity detrimental to India's interest.

It is noteworthy that the Government, at this stage, only intends to prescribe disclosure requirements. It neither wishes to expressly restrict/prohibit such investments by a clarification in the FDI Policy, nor does it intend to prescribe for "prior permission/approval" of the Government for such investments. It, therefore, seems improbable that the Government would ask any of the investors to disinvest or discontinue on a future date. Consequently, the purpose of the disclosures seem only to be of 'record keeping' by the Government.

In that light, the disclosure itself may not be required, as similar disclosures are more or less required even today as part of Know Your Customer norms/ Anti-Money Laundering standards/Combating of Financing of Terrorism and the directions of the Reserve Bank of India and provisions of PML Act. The investee Indian company would also provide details of its shareholders once it commences any banking relationship, and the Indian investing company may have, in any case, given the requisite particulars of its shareholders at the time of receiving investments from them.

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