

Issues for offshore investment funds: To declare or not to declare

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To curb money laundering or *benami* transactions, the government recently amended the Companies Act, 2013, and altered the framework for determining beneficial interest and ownership under Section 89 and 90 of the Act, by introducing the Companies (Significant Beneficial Owners) Rules, 2018.

Section 89 defines "beneficial interest" as "if any person

other than the legal owner of the share(s) has the ability to enforce or cause the enforcement of any rights attached to the share(s), whether in the nature of participation in decision making or dividend or otherwise either through a contract, arrangement or otherwise".

It requires that if any person

other than the legal owner has beneficial interest in the share(s), then appropriate declarations should be made by the legal owner and the holder of beneficial interest.

To clarify, if the legal owner and the holder of beneficial interest is the same person, no filings are required under Sections 89 and 90. In case of investment funds, which have delegated voting rights to its investment manager (managed funds), the asset manager

COMMENTARY

will be required to be disclosed as the holder of beneficial interest. For instance, FPIs, which buy on a daily basis, may be required to make a filing for every purchase, which is inane and cannot be the intent of law.

In our view, Section 90 progresses from Section 89 and sets out that if beneficial interest has been identified, then the investee company should



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seek to identify the individual (a) who holds "ultimate beneficial interest" of 10% or more; and (b) whose name is not entered in the register of members. Such an individual is referred to as the significant beneficial owner (SBO).

Legislative intent appears to first identify who holds beneficial interest (in Section 89) and then identify an individual as

the SBO of such beneficial interest (in Section 90).

In case of managed funds, the manager will hold beneficial interest. In such a situation, one will need to identify whether there is a natural person that holds 10% or more shares, or exercises significant influence and/or control over the shares, of the manager. Such natural person shall be the SBO. If, however, there is no natural person in the whole chain, one will need to identify senior managing official of the manager as its SBO.

Interestingly, Section 90 and the Companies Rules, exempt "pooled investment vehicles and/or investment funds such as mutual funds, AIFs, REITs and InvITs regulated by SEBI".

The inclusive language of the exemption leaves one to guess whether the regulator intended to cover other Securities and Exchange Board of India or Sebi-regulated enti-

ties, such as FPIs or FVCIs, to be exempt from making SBO declarations.

Keeping the spirit of the regulation in mind, it does seem that Sebi-registered vehicles should also be exempt as they have their own set of ownership disclosures, which are made to the Sebi in the prescribed formats.

It is also important to understand that in case of a failure to disclose beneficial interest by the holder of beneficial interest, such holder of beneficial interest will not be able to enforce its rights under Section 89. Further, under Section 90, Indian companies can also be called into question if they, despite having knowledge that beneficial interest is held by someone other than the legal owner, do not question the shareholder or take any action in such respect.

Hence, today, it is incumbent upon Indian companies to ask questions to its share-

holders, and for the legal owner of shares of Indian companies to evaluate their contracts to ascertain whether by virtue of their contract, any beneficial interest is being created in favour of a third party.

While Section 89 has been in effect, filings under Section 90 were to be made, effective 11 September. However, based on industry representations, the government is considering revising the form under which SBO disclosures are required. Filings under Section 90 have also been deferred. Notwithstanding its teething issues, the requirement of identifying the SBO will remain and investment funds should prepare themselves on such disclosures accordingly.

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