



**The Chamber of
Tax Consultants**
Mumbai | Delhi

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Imm. Past President
Hinesh R. Doshi

10th October, 2019

To,
Shri Rajesh Gujjar
General Manager
Corporation Finance Department
Securities and Exchange Board of India,
SEBI Bhavan, Plot No.C4-A, 'G' Block,
Bandra-Kurla Complex,
Bandra (East),
Mumbai - 400051

**Subject: Request for clarification on matters arising out of change in
definition of "Encumbrance"**

Respected Sir,

The Chamber of Tax Consultants (CTC), Mumbai was established in 1926. CTC is one of the oldest voluntary non-profit making organizations in Mumbai – in its 93rd year - formed with the object of educating and updating its members on Tax and other Laws. It has robust membership strength of about 4000 professionals, comprising Advocates, Chartered Accountants and Tax Practitioners. The Chamber also has created a niche with the government and other regulatory agencies. It is the one of the leading institution for making effective representation with respect to Income Tax and Allied laws. It acts as catalyst for bring out necessary change both from the perspective of Government as well as Tax payers.

We appreciate the efforts taken by SEBI for tightening the definition of "Encumbrance" and the introduction of new disclosures, which will go a long way in bringing transparency in the Securities market and curb malpractices done by few promoters of listed companies.

However, with these new amendments, a few queries arose from our members. Hence, we are writing for seeking your clarification with regard to the following points:-

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A. Amendment in Definition of “Encumbrance”

1. Change in definition –

Pursuant to an amendment in SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 (“SEBI SAST Regulations”) dated 29th July 2019, the definition of “encumbrance” has been amended to include following new items under the definition of “encumbrance”:-

- **any restriction on the free and marketable title to shares**, by whatever name called, whether **executed directly or indirectly**;
- **pledge, lien, negative lien, non-disposal undertaking**;
- any covenant, transaction, condition or arrangement in the nature of encumbrance, by whatever name called, whether executed directly or indirectly.

2. So, following questions have arose among various listed companies:-

I. Coverage under the new definition of “encumbrance”

- (i) Whether lock-in of shares will be covered in the new definition of “encumbrance”, as it is a restriction on the free and marketable title of shares?
- (ii) Whether “tag-along”, “drag-along” or “pre-emption” provisions in Agreements entered into by Promoters of listed companies with Investors with regard to the shares held by promoters in listed companies will also be covered in the new definition of “encumbrance”?

II. Impact under other SEBI Regulations

- (i) Under SEBI (LODR) Regulations, under Regulation 31, a disclosure of Shareholding pattern is to be submitted to Stock Exchanges on quarterly basis. In the format of that disclosure, listed companies need to disclose whether any of the shares held by promoters and promoter group entities are pledged **or otherwise encumbered**.



So, should **all such items which are covered under the new definition of “encumbrance”** (like non-disposal undertaking, negative lien etc) **also be disclosed in the Quarterly Shareholding Patterns** filed by listed companies under the column of “Shares pledged or otherwise encumbered”?

- (ii) Under SEBI (Prohibition of Insider Trading) Regulations, 2015, (“SEBI PIT Regulations”), the definition of “trading” is defined as “trading” means and includes subscribing, buying, selling, **dealing**, or agreeing to subscribe, buy, sell, deal in any securities, and “trade” shall be construed accordingly.

In the Note given under this definition in SEBI PIT Regulations, it is mentioned that ***“it is intended to widely define the term “trading” to include dealing. Such a construction is intended to curb the activities based on unpublished price sensitive information which are strictly not buying, selling or subscribing, such as pledging etc when in possession of unpublished price sensitive information.”***

So, if “pledging” of shares will be covered under the term “dealing” and hence covered under the term “trading” under SEBI PIT Regulations, **does it mean that other items in the new definition of “encumbrance” like non-disposal undertaking, negative lien etc will also be covered under the purview of SEBI PIT Regulations?**

B. Disclosure of reasons of “Encumbrance” in case of crossing threshold limits:

1. SEBI Circular mandating the new disclosure requirement -

SEBI has, vide Circular dated 7th August 2019, mandated the new requirement for disclosure of reasons and other details in cases where the combined encumbrance created by the promoter / promoter group entities of listed company along with PACs equals or exceeds:

- a) 50% of their shareholding in the company; or
- b) 20% of the total share capital of the company,



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2. Initial Disclosure Requirement

As per the said circular, in all cases where the above thresholds are already crossed as on 30th September 2019, a disclosure needs to be given by 4th October 2019.

3. Continual Disclosure Requirement

Thereafter, this disclosure of reasons of encumbrance and other details is to be given **on every occasion** when the extent of encumbrance (having already breached the above threshold limits) increases further from the prevailing levels. This disclosure is to be given **within two working days from the date of creation of encumbrance.**

4. So, following questions have arose among various listed companies:-

- (i) The existing disclosure to be given by promoter on creation of encumbrance under Reg 31(1) of SEBI SAST Regulations is to be given within 7 working days from date of creation of encumbrance. This new disclosure is to be given within 2 working days from date of creation of encumbrance.

So, if the new disclosure is to be given within 2 working days from date of creation of encumbrance, then what is the need of giving another disclosure under Reg 31(1) of SEBI SAST Regulations within 7 working days?

- (ii) There can be many cases where a promoter has given “Non Disposal Undertaking” for his entire shareholding to one lender against a Credit facility Arrangement, and the Initial Disclosure as on 30th September 2019 is given to stock exchanges and Company.



Thereafter if the credit facility is renewed and hence new agreement is signed with the lender (containing Non Disposal Undertaking as one of the clauses of the Facility Agreement), will it amount to increase in encumbrance from the prevailing levels and warrant the requirement of disclosure again?

C. Yearly Declaration to be given by promoters regarding Encumbrance Creation:

Pursuant to an amendment in SEBI SAST Regulations dated 29th July 2019, Reg 31(4) and Reg 31(5) have been inserted in the SEBI SAST Regulations which require every listed company to *“declare on a yearly basis that he, along with persons acting in concert, has not made any encumbrance, directly or indirectly, other than those already disclosed during the financial year”*

This declaration is to be made to every stock exchange where the shares of the target company are listed; and to the audit committee of the target company, within 7 working days from the end of financial year. However, the format in which this declaration is to be given is not specified by SEBI.

So, does it mean that this declaration is to be given as a part of the disclosure under Regulation 30(2) – Continual Disclosures, which are to be given by every promoter for disclosing the aggregate shareholding and voting rights held by the promoter together with persons acting in concert with him as on 31st day of March every year, which is also to be given within 7 working days from the end of financial year. If yes, then the format of such disclosure under Regulation 30 needs to be amended to include this declaration.

If it need not for part of the Continual Disclosures under Regulation 30, then we request you to kindly specify a format for this declaration, so as to bring clarity among the promoters of listed companies.



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We wish to submit you to please clarify on the above points at the earliest so as to bring clarity on these provisions among the listed companies and their promoters.

Thanking you,

Sincerely yours,

For **THE CHAMBER OF TAX CONSULTANTS**

Sd/-

VIPUL K. CHOKSI
PRESIDENT

Sd/-

MAHENDRA SANGHVI
CHAIRMAN
LAW & REPRESENTATION COMMITTEE

Sd/-

APURVA SHAH
CO-CHAIRMAN