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IRDAI ISSUES CLARIFICATIONS ON TRANSFER OF SHARES OF INSURERS

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The Insurance Regulatory and Development Authority of India (IRDAI) on 22 July 2020, issued a circular to all insurance companies, in relation to the transfer of shares of insurance companies (Circular). The Circular has been issued to bring greater clarity to the existing provisions governing the transfer of shares of insurers, being: (a) section 6A of the Insurance Act 1938 (Insurance Act); (b) IRDAI (Transfer of Equity Shares of Insurance Companies) Regulations 2015 (Transfer Regulations); and (c) IRDAI (Listed Indian Insurance Companies) Guidelines dated 5 August 2016 (ListCo Guidelines).

The Circular deals with 4 critical aspects pertaining to share transfers, ie: (a) intimation and approval requirement for transfer of shares of listed insurers; (b) time period for determining transfer thresholds; (c) pledge of shares of insurers; and (d) suspension of voting rights. We have analysed the key changes brought forth pursuant to the Circular.

A. Intimation and Approval Requirement for Transfer of Shares of Listed Insurers

- (i) Intimation to IRDAI: Currently, as per the ListCo Guidelines, for any transfer of shares amounting to more than 1% but less than 5% of the paid-up share capital of a listed insurer (Notifiable Transaction), the acquirer is required to submit a 'Fit and Proper' declaration to the relevant listed insurer. The self-certification is deemed to be an approval of IRDAI for such transfer, under the Insurance Act.

The IRDAI has, *vide* the Circular, reiterated this requirement and has additionally imposed a requirement on the transferor as well, to 'immediately' intimate the insurer on the execution of a Notifiable Transaction.

- (ii) Prior Approval of IRDAI: Currently, as per the ListCo Guidelines, in case of transfer of shares where pursuant to a transfer, the acquirer's (along with relatives, associate enterprises and/or persons acting in concert (**PAC**)) aggregate shareholding in the listed insurer is likely to exceed 5% of paid-up share capital of the insurer, the acquirer is required to obtain prior approval of IRDAI.

The IRDAI, *vide* the Circular has reiterated this requirement and has also imposed an obligation on the transferor to obtain prior approval of IRDAI

in case such transfer of shares (including transfer(s) by PAC) is likely to exceed 5% of the paid-up share capital of the listed insurer.

The Circular clarifies that transactions involving sale of shares amounting to 5% or more of the paid-up capital of a listed insurer by any transferor (including its PAC) will require prior approval of IRDAI, irrespective of whether pursuant to such transfer, any of the acquirers' shareholding in such listed insurer, exceeds 5% of the paid-up capital. It is, however, unclear whether two separate applications would have to be made to IRDAI, for transactions triggering approval requirements vis-à-vis both the transferor and the acquirer. Further, the Circular is silent on the intimation / approval requirements for transactions involving further acquisition of shares by a shareholder holding 10% of the paid-up share capital of a listed insurer, as required under the ListCo Guidelines.

B. Time Period for Determining Transfer Thresholds

The Circular specifies that for determining the requirement to notify IRDAI / insurer or seek prior approval of IRDAI, all transactions executed during a particular financial year will have to be considered (FY Threshold). While this requirement is applicable to all shareholders of unlisted insurers, in the case of listed insurers it is restricted to promoters and promoter group. In such a scenario, given the possibility of numerous buy-sell on-market transactions, it will be interesting to see if the FY Threshold is applied as a net of all buy-sell transactions undertaken by the promoter groups per financial year, or if only all sales undertaken by the promoter group are aggregated.

Additionally, the Circular clarifies that for listed insurers, 'transfer' includes an 'offer for sale' (as determined under extant SEBI regulations) by any shareholder.

While in case of listed insurers, as per the ListCo Guidelines and the Circular, the onus of intimation / seeking approval (as the case may be) is on the transferor and acquirer, in case of unlisted insurers, an application seeking approval of IRDAI, as per the Transfer Regulations, is to be made by the relevant insurer. Further, the Circular mentions that in case of breach of FY Threshold, the "entity" would be responsible for obtaining prior approval of IRDAI. Accordingly, the usage of the term "entity" may be interpreted as IRDAI obligating the insurers (in addition to shareholders) to track share transfers and allotments which may result in breach of the FY Threshold.

C. Pledge of Shares

As per the Circular, the creation of pledge or any form of encumbrance on the shares of an insurer, by its promoters, will now require prior approval of IRDAI in accordance with the provisions set out in section 6A(4) of the Insurance Act and the Transfer Regulations. Accordingly, the promoters of insurers whose shareholding is currently pledged may have to seek post-facto approval of IRDAI, pursuant to the Circular.

It is interesting that such an approval requirement is only applicable in case of creation of pledge or encumbrance by a promoter and has not been extended to other shareholders. At present, private equity investors are prohibited from creating any encumbrance on their shareholding in unlisted insurers.

D. Suspension of Voting Rights

The Circular places the obligation on the insurer to: (a) ensure compliance with the Insurance Act, Transfer Regulations and ListCo Guidelines; and (b) intimate

IRDAI in case of any non-compliance with these provisions, with respect to the transfer of shares of the insurer. The Circular further prescribes that in case of any transfer beyond the stipulated threshold without IRDAI approval, the acquirer: (x) will not have any voting rights in relation to such shares; and (y) shall promptly be required to dispose of its shareholding beyond the specified threshold.

Conclusion

The changes and clarifications introduced by IRDAI appear to be emanating from its recent experience and learnings. For instance, the requirement for transferors of shares of listed insurers to notify / seek approval of IRDAI is a regulatory change to incorporate the recent IRDAI order in the matter of SBI Life Insurance Company Limited, where, IRDAI had clarified that in case of transfer of shares constituting more than 5% of the shareholding of a listed insurer, irrespective of the obligations of the acquirer, the transferor is required to obtain approval in accordance with the Insurance Act, Transfer Regulations and ListCo Guidelines.

With respect to the change pertaining to pledge of shares, the clarification that 'transfer' includes within its ambit creation of pledge or any form of encumbrance over shares of an insurer, is a direct consequence of a recent case involving the pledge of shares of an insurer. In this case, IRDAI's initial ruling on the invocation of such pledge being null and void was subsequently overruled by the Securities Appellate Tribunal.

While IRDAI has left a few questions unanswered, the Circular provides much needed clarity with respect to existing provisions on transfer of shares and reflects the regulator's intent to address issues arising out of current market transactions. However, the procedural aspects of some of these changes introduced by IRDAI through the Circular are awaited.

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