



**MCA INTRODUCES  
AMENDED RULES FOR  
SIGNIFICANT  
BENEFICIAL OWNERSHIP**

**February 11, 2019**

**argus**  
**partners**  
SOLICITORS AND ADVOCATES

## Introduction

On February 8, 2019, the Ministry of Corporate Affairs (“MCA”) issued a notification in respect of the Companies (Significant Beneficial Owners) Amendment Rules, 2019 (“Amendment Rules”) to amend the Companies (Significant Beneficial Owners) Rules, 2018 (“Rules”).

The Rules have been formulated under section 90 of the Companies Act, 2013 (“CA 2013”), which provides the disclosure requirements for significant beneficial owners in a company. Section 90 and the Rules were notified in June 2018, in line with the recommendations of the Financial Action Task Force (“FATF”) for combating money laundering and the financing of terrorism. The FATF had recommended that countries should take measures to prevent the misuse of legal persons for money laundering or terrorist financing and ensure that there is adequate, accurate and timely information on the beneficial ownership and control of legal persons, which can be obtained or accessed in a timely fashion by competent authorities.

However, subsequently the MCA received representations from various stakeholders on difficulties in filing the declaration under the Rules. In view of the stakeholders’ concerns, the requirement of filing the declaration under the Rules was stayed until the revised form was issued by the MCA for the same.<sup>1</sup>

The Amendment Rules will come into force on the date of their publication in the Official Gazette.

This paper discusses the amendments proposed to the Rules and some of the issues which may require further clarity.

## Meaning of ‘significant beneficial owner’

Section 90 of CA 2013 provides that every ‘significant beneficial owner’ is required to make a declaration to the company (“Relevant Company”), specifying the nature of her interest and other particulars, in the prescribed manner.

The term ‘significant beneficial owner’ has been defined in section 90 of CA 2013 as any individual, acting alone or together with others (including trusts and persons resident outside India), who –

- (i) holds beneficial interests, of not less than 25% or such other prescribed percentage, in the shares of the Relevant Company; or
- (ii) holds the right to exercise, or the actual exercising of significant influence or control<sup>2</sup> over the Relevant Company.

However, the amended Rules<sup>3</sup> provide a different definition of a ‘significant beneficial owner’. As per the definition introduced in the amended Rules, a ‘significant beneficial owner’ is an individual, acting alone or together with others, who possesses one or more of the following rights or entitlements in the Relevant Company:

- (i) holds indirectly, or together with any direct holdings, not less than 10% of the shares;
- (ii) holds indirectly, or together with any direct holdings, not less than 10% of the voting rights in the shares;

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<sup>1</sup> General Circular No. 08/2018 dated September 10, 2018 issued by the MCA.

<sup>2</sup> The term ‘control’ has been defined in section 2(27) of CA 2013 as follows:

*"control" shall include 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.*

<sup>3</sup> Rule 2(1)(h) of the amended Rules.

- (iii) has the right to receive or participate in not less than 10% of the total distributable dividend, or any other distribution, in a financial year through indirect holdings alone, or together with any direct holdings;
- (iv) has the right to exercise, or actually exercises, significant influence or control, in any manner other than through direct holdings alone.

The amended Rules<sup>4</sup> further explain that if an individual does not hold any indirect right or entitlement as mentioned in (i), (ii) or (iii) above, she will not be considered to be a 'significant beneficial owner'. This appears to be a clarification to the effect that until and unless an individual has any indirect (as opposed to direct) right or entitlement as mentioned in (i), (ii) or (iii) above, she will not constitute a 'significant beneficial owner'. The explanation seems to be merely clarificatory in nature since the definition, in any event, mandatorily stipulates an indirect holding/ right under (i), (ii) or (iii) above and the direct holding/ right may be optional but in addition to such indirect holding/ right.

### **Significant influence**

The amended Rules define 'significant influence' as the power to participate in the financial and operating policy decisions of the Relevant Company, but not being in control or joint control of the Relevant Company.<sup>5</sup>

This is different from the definition of 'significant influence' for the purposes of the meaning of 'associate company' under CA 2013. For that purpose, 'significant influence' has been defined to mean control of at least 20% of total voting power, or control of or participation in business decisions under an agreement.

An interesting issue which may arise is the scope of the phrase '*participate in the financial and operating policy decisions of the Relevant Company*'. Whilst the term 'participate' is not defined in the amended Rules, as in the case of the definition of 'associate company' as stated above, a plain reading may lead to an interpretation where merely having nominee directors or certain affirmative veto rights on financial and operating policy decisions of a company or quorum rights may be considered to be exercising 'significant influence'.

### **Acting together**

Individuals, acting either by themselves or through any person or trust, shall be deemed to be 'acting together' if they act with a common intent or purpose of exercising any right or entitlement or exercising control or significant influence over the Relevant Company, pursuant to an agreement or understanding, whether formal or informal.<sup>6</sup>

### **Direct right or entitlement**

An individual will be considered to hold a right or entitlement directly in the Relevant Company, if she satisfies any of the following criteria:<sup>7</sup>

- (i) the shares in the Relevant Company representing such right or entitlement are held in the name of such individual;
- (ii) the individual holds or acquires a beneficial interest in the shares of the Relevant Company under section 89(2) of the CA 2013, and has made a declaration in this regard to the Relevant Company.

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<sup>4</sup> Explanation I to Rule 2(1)(h) of the amended Rules.

<sup>5</sup> Rule 2(1)(i) of the amended Rules.

<sup>6</sup> Explanation V to Rule 2(1)(h) of the amended Rules.

<sup>7</sup> Explanation II to Rule 2(1)(h) of the amended Rules.

## **Indirect right or entitlement<sup>8</sup>**

### *Body corporate*

An individual will be considered to hold a right or entitlement indirectly in the Relevant Company through a body corporate (other than a limited liability partnership), where such individual (a) holds majority stake<sup>9</sup> in the body corporate; or (b) holds majority stake in the ultimate holding company of the body corporate.

### *HUF*

An individual will be considered to hold a right or entitlement indirectly in the Relevant Company through a Hindu Undivided Family (HUF), where such individual is the *karta* of the HUF.

### *Partnership*

An individual will be considered to hold a right or entitlement indirectly in the Relevant Company through a partnership, where such individual (a) is a partner; or (b) holds majority stake in the body corporate which is a partner; or (c) holds majority stake in the ultimate holding company of the body corporate which is a partner.

### *Trust*

An individual will be considered to hold a right or entitlement indirectly in the Relevant Company through a trust, where such individual is (a) a trustee (in case of a discretionary trust or a charitable trust); or (b) a beneficiary (in case of a specific trust); or (c) the author or settlor (in case of a revocable trust).

### *Pooled investment vehicles*

An individual will be considered to hold a right or entitlement indirectly in the Relevant Company through a pooled investment vehicle or an entity controlled by a pooled investment vehicle, where such individual is a (a) general partner; or (b) investment manager of such pooled investment vehicle; or (c) Chief Executive Officer (where the investment manager is a body corporate or a partnership).

However, this will be applicable only in cases where such pooled investment vehicle or entity controlled by a pooled investment vehicle is based in a member State of the FATF and the securities market regulator of such State is a member of the International Organisation of Securities Commissions. In all other cases, the criteria applicable to body corporates, HUFs, partnerships or trusts, as the case may be, will apply.<sup>10</sup>

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<sup>8</sup> Explanation III to Rule 2(1)(h) of the amended Rules.

<sup>9</sup> The term 'majority stake' has been defined in rule 2(1)(d) of the amended Rules to mean:

- (i) holding more than one-half of the equity share capital in the body corporate; or
- (ii) holding more than one-half of the voting rights in the body corporate; or
- (iii) having the right to receive or participate in more than one-half of the distributable dividend or any other distribution by the body corporate.

<sup>10</sup> Explanation IV to Rule 2(1)(h) of the amended Rules.

## Declaration of significant beneficial ownership

Every individual who is a significant beneficial owner in the Relevant Company, as on the date of commencement of the Amendment Rules, is required to file a declaration with the Relevant Company in Form BEN-1 within 90 days from such commencement.<sup>11</sup>

Any individual, who subsequently becomes a significant beneficial owner in the Relevant Company or whose significant beneficial ownership undergoes any change, is required to file a declaration with the Relevant Company in Form BEN-1 within 30 days of such acquisition or change.<sup>12</sup>

If an individual becomes a significant beneficial owner in the Relevant Company or her significant beneficial ownership undergoes any change during the aforesaid 90 day period, such individual will be required to file a declaration with the Relevant Company in Form BEN-1 within 30 days of expiry of the aforesaid 90 day period.<sup>13</sup>

## Duties of companies

Once the Relevant Company receives the declaration from a significant beneficial owner, it is required to file a return in Form BEN-2 with the Registrar of Companies, within 30 days of receipt of such declaration.<sup>14</sup>

The amended Rules also cast an obligation on the Relevant Company to take necessary steps to find out its significant beneficial owners and cause such individuals to file a declaration in Form BEN-1.<sup>15</sup>

It would need to be seen what necessary steps a company can take to effectively carry out the obligation of finding out its significant beneficial owners, especially in cases where persons may be acting together without the knowledge of the company.

Further, in addition to the aforesaid general obligation, where the member (not being an individual) of the Relevant Company holds not less than 10% of shares or voting rights or the right to receive or participate in the dividend or any other distribution payable in a financial year, the Relevant Company is required to give notice to such member seeking information on the beneficial ownership of such member.<sup>16</sup>

## Non-applicability

The amended Rules will not be applicable where the shares of the Relevant Company are held by:<sup>17</sup>

- (i) the Investor Education and Protection Fund Authority;
- (ii) its holding company which has complied with section 90 of CA 2013 and the Rules, provided that the details of such holding company are reported in Form BEN-2;
- (iii) the Central Government, any State Government or any local authority;

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<sup>11</sup> Rule 3(1) of the amended Rules.

<sup>12</sup> Rule 3(2) of the amended Rules.

<sup>13</sup> Explanation to rule 3(2) of the amended Rules.

<sup>14</sup> Rule 4 of the amended Rules.

<sup>15</sup> Rule 2A(1) of the amended Rules.

<sup>16</sup> Rule 2A(2) of the amended Rules.

<sup>17</sup> Rule 8 of the amended Rules.

- (iv) an entity/ body corporate controlled wholly or partly by the Central Government and/ or State Government(s);
- (v) investment vehicles such as mutual funds, alternative investment funds (AIFs), Real Estate Investment Trusts (REITs) and Infrastructure Investment Trusts (InVITs) registered with and regulated by the Securities and Exchange Board of India; and
- (vi) investment vehicles regulated by the Reserve Bank of India, Insurance Regulatory and Development Authority of India or Pension Fund Regulatory and Development Authority.

## Conclusion

Most of the major concerns which emanated from the Rules, as notified in June 2018, seem to have been addressed. For instance, the Rules initially provided that where the member is a company/ partnership firm having significant beneficial ownership, and no individual is identified as a significant beneficial owner, the senior managing official of such company/ partnership firm would be considered as the significant beneficial owner. Also, in cases where the member is a trust, the author and trustee of the trust would be considered as the significant beneficial owners, irrespective of the nature of the trust (discretionary/ non-discretionary or revocable/ irrevocable). These provisions have been dropped in the amended Rules.

However, there are still certain unaddressed issues which may be faced by investors as well as companies. Specifically impacted will be the private equity/ venture capital investors who are not registered with the Indian regulators. The issue on what would be the extent of the '*participation in financial and operating policy decisions*' to qualify as '*significant influence*' would need further consideration, as it is fairly common for private equity/ venture capital investors to have nominee directors, affirmative rights on financial and operating policy decisions of a company as per their investment agreement. Further, the obligation imposed on companies to '*take necessary steps to find out*' their significant beneficial owners, especially where persons are '*acting together*' without the knowledge of the company, may be difficult to fulfil.

*This note has been written by Krishnava Dutt (Managing Partner) and Aastha (Partner).*

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