ENFORCEABILITY OF PRE-EMPTION RIGHTS / CALL & PUT OPTION

Any foreign investor intending to make an investment in the equity share capital of any company in India prefers to have an exit option (call & put option) under the transaction document(s). An exit option generally gives flexibility to the foreign investor(s) to sell the securities in the event of (i) the project for which money is infused in India is unsuccessful; or (ii) there is a dispute between the foreign investor and the Indian party in relation to the operation of the company or a project; or (iii) there is a change in the policies of the Government of India; or (iv) the foreign investor does not want to remain invested in the company due to any other reason.

In addition to the aforesaid exit option, the parties to the transaction documents also prefer to have some pre-emptive rights such as the right of first refusal, tag-along or drag-along rights due to some commercial reasons or in order to protect their interest. The legal enforceability of such pre-emptive rights in India including call & put option shall always be the concern of foreign investors. In this article, I have tried to analyze all the relevant legal issues in relation to the enforceability of the aforesaid options including the provisions of the Companies Act, 2013 (“**CA 2013**”), notifications issued by the Securities and Exchange Board of India (“**SEBI**”) and the Reserve Bank of India (“**RBI**”) in this regard.

It was well established under the provisions of the Companies Act, 1956 (“**CA 1956**”) that any provision contained in any agreement executed between a company and a third party so far it is inconsistent with the provisions of the CA 1956 shall be void. However, in order to bind the company and all the shareholders inter-se, the foreign investor prefers to incorporate the relevant terms of their consensual arrangement (such as shareholders’ agreement) in the Articles of Association of a company (“**AoA**”).

As far as the new CA 2013 is concerned, there is no change under the aforesaid legal position under the said Act. Section 6 (Act to override memorandum, articles, etc.) and Section 10 (Effect of memorandum and articles) of CA 2013 continue to give effect to the aforesaid legal position.

In order to further analyze the enforceability of the aforesaid options, this Article is divided into three parts:

- Pre-emption Rights relating to transfer of shares;
- Pre-emption Rights relating to issue of shares by the company; and
- Call & Put Option.

Pre-emption Rights relating to transfer of shares

Meaning

A pre-emptive right in respect of transfer of shares is essentially a right to impede the transfer / sale of shares to a third party, and demand that such shares be transferred / sold to the agreed party(ies) / shareholder(s).

Relevant Provisions of CA 1956 & CA 2013

In terms of the provisions of CA 2013:

(i) A private company is required to restrict the transfer of its shares through its AoA [**Section 2(68) of CA 2013**].

(ii) If a private company refuses to, whether in pursuance of any power of the company under its AoA or otherwise, register the transfer of any securities or interest of a member, it is required to intimate the transferor and transferee within the stipulated time period [**Section 58 of CA 2013**]. It is to be noted that as far as the provisions of CA 2013 and the erstwhile CA 1956 are concerned; there is no change in the aforesaid legal position of a private limited company providing restriction on transfer of its shares through its AoA. Such a restriction will continue to be valid and binding on such private company and its members under the new CA 2013.

(iii) However, there were some debatable issues under the erstwhile CA 1956, in relation to the restriction on the transfer of shares by public companies, keeping in mind the provisions of Section 111A of erstwhile CA 1956, which made the shares of a public company '**freely transferable**'.

(iv) Section 58 (2) of CA 2013 provides that '**without prejudice to Sub-Section 58 (1)**', the securities or other interest of any member in a public company shall be '**freely transferable**' (emphasis supplied). Further, proviso to Section 58 (2) of CA 2013 provides that any contract or arrangement between two or more persons in respect of transfer of securities shall be enforceable as '**contract**'. The provisions of Section 58 (2) of CA 2013 are similar to the provisions of Section 111A of the erstwhile CA 1956 except the proviso to Section 58 (2) of CA 2013 as mentioned above.

It must be noted that the proviso to Section 58(2) of the CA 2013 is in line with the judgment of the Bombay High Court in the matter of **Messer Holdings Limited vs Shyam Madanmohan Ruia & Others [2010 159CompCas29(Bom)]**. As per the Bombay High Court, any contract or arrangement between two or more persons with respect to transfer of securities can be enforced like any other contract and does not impede the free transferability of shares at all.

Hence, any consensual arrangement between the shareholders, in relation to the shares of a public company, shall be valid and binding as a '**contract**' inter-se the shareholders. If any public company is also being made party to such a consensual arrangement / contract, then such a contract will also be enforceable against the public company as a '**contract**' in terms of the proviso to Section 58(2) of the CA 2013. In case of breach of such a contract by any party, the aggrieved party may avail legal remedies as available in case of 'breach of contract' including specific performance of the contract under the Specific Relief Act, 1963.

Expression 'Free Transferability'

The expression '**freely transferable**' is not defined under the CA 2013. However, Section 58(4) of CA 2013, provides that if a company without '**sufficient cause**' refuses to register the transfer of shares, the transferee may appeal to the National Company Law Tribunal ("**NCLT**") and the NCLT shall direct such a company to register the transfer of shares in terms of the provisions of Section 58(5) of CA 2013.

The board of directors, upon '**sufficient cause**' being seen, may refuse to register the transfer of shares. The words '**sufficient cause**' in Section 58(4) takes within its ambit not only those contingencies contemplated under sub-section (3) but also circumstances and reasons other than which might require the company to refuse to register the transfer of shares. Thus, there can be various reasons, though it is not possible to enumerate all of them and dependant on the facts of each case, which would constitute '**sufficient cause**' for a company to refuse the registration of transfer of shares.

Messer Holdings Judgement

The Hon'ble High Court of Bombay in **Messer Holdings Limited vs Shyam Madanmohan Ruia & Others** [2010 159CompCas29 (Bom)], while dealing with the question of validity of an agreement having a first right of refusal (pre-emption right), inter-alia observed that:

"…For that, we may have to consider the objects and reasons for which Section 111 A has been introduced in the Companies Act. Prior to the introduction of Section 111 A, Section 111 of the Companies Act, 1956 provided for the remedy of appeal to a transferor or transferee seeking relief in respect of a transfer / transmission of shares in a public or private company.

They could apply for rectification of register of members under Section 155.

With effect from January 17, 1986, Section 22 A was inserted in the Securities Contracts (Regulations) Act, 1956. It provided that the shares of the registered company be made freely transferable. However, the company could refuse transfer only on four specified grounds. The said provision was introduced in the backdrop of a series of complaints regarding arbitrary powers exercised by the Board of Directors in refusing or non-consideration of request for transfer/transmission of shares in favour of the transferee. It thus follows that the provisions of Section 22A of the Securities Contracts (Regulation) Act 1956 was intended to regulate the right of the Board of Directors of the company to refuse transfer of shares. **That was not a provision to restrict the right of shareholders to deal with their shares or to enter into consensual arrangement / arrangement regarding their shares (by way of pledge, pre-emption, sale or otherwise). Suffice it to observe that the intention behind introducing Section 22 A in 1986 was to regulate the right of the Board of Directors to refuse transfer of member's share and it was not to impose restriction on the right of the shareholder to deal with his shares by entering into a consensual arrangement with the third party to which the company need not be a party**."

"51(7)…..… In other words, the setting in which Section 111A is placed in part IV of the Act under the heading "transfer of shares and debentures", it is not a provision to curtail the rights of the shareholders to enter into a consensual arrangement with the purchaser of their specific shares. The right to enter into a consensual arrangement must prevail as long as it is in conformity with the terms of Articles of Association and other provisions of the Act and the Rules. Whereas, Section 111A is a provision mandating the Board of Directors of the company to transfer shares in the name of the transferee, subject to the stipulations in Section 111A of the Act. **The expression "freely transferable" therein is in the context of the mandate against the Board of Directors to register the transfer of specified shares of the members in the name of the transferee, unless there is sufficient cause for not doing so**. The said provision cannot be construed to mean that it also intends to take away the right of the shareholder to enter a consensual arrangement/contract with the purchaser of their specific shares. If the legislature intended to take away that right of the shareholder, it would have made an express provision in that regard. Reliance has been rightly placed on the decision of the Apex Court in the case of Byram Pestonji Gariwala (supra) which takes the view that the freedom of contract generally, the legislature does not interfere except when warranted by public policy, and the "legislative intent is expressly made manifest…………"

In view of the aforesaid judgement:

(i) The expression '**freely transferable**' should be given wider interpretation and any consensual arrangement / contract providing pre-emptive rights pertaining to transfer of shares should not be construed as violation of the expression '**freely transferable**'. Had that not been the intention of the legislature, the proviso to Section 58(2) of the CA 2013 would not have been specifically inserted and appropriate restriction would have been placed in the CA 2013 in relation to transfer of shares in terms of consensual arrangement; and

(ii) The expression '**freely transferable**' is a mandate against the board of directors to register the transfer of the specified shares. However, such expression does not in any way way restrict the power of the board of directors of a public company to refuse the registration of transfer of such shares on '**sufficient cause**'.

As far as a private company is concerned, such a private company is permitted to insert restrictions on transfer of shares in its AoA in terms of provisions of Section 2(68) and Section 58(1) of CA 2013. Hence, any restriction on transfer of shares as agreed under the consensual arrangement shall be valid and binding on such a private company and it may be duly incorporated in the AoA and may be enforced against the shareholders of a private company.

Pre-emption Rights relating to issue of shares by a company

Meaning

A pre-emptive right in respect of issue of new shares is essentially a right entitling the existing shareholder(s) or agreed shareholder(s) to acquire further shares to be issued by a company. In the event of such shares not acquired by the existing shareholder(s) or agreed shareholder(s), such shares shall be dealt with in the manner as provided in AoA of the company and in accordance with the provisions of the CA 2013.

Relevant Provisions of CA 1956 and CA 2013

Section 62 of CA 2013 deals with issue of further shares by the company. Where at any given time, in terms of said section 62, a company having a share capital proposes to increase its subscribed capital by issue of further shares, such shares shall be offered to:

(i) The existing shareholders;
(ii) The employees under employee stock option scheme; and
(iii) Any other person;

in compliance with the applicable rules.

In the erstwhile CA 1956, there was a distinction between a 'public limited company' and a 'private limited company' in relation to the issue of shares on preferential basis. The provisions of Section 81 of the erstwhile CA 1956, dealing with preferential issue of shares, were not applicable to a private limited company. However, under CA 2013,no such distinction has been made and the provisions of Section 62 of CA 2013, dealing with preferential issue of shares, are made applicable to a 'public limited company' as well as a 'private limited company'.

In view of the aforesaid position of Section 62 of the CA 2013, a company may issue further shares to a particular class of shareholder(s) / third party in preference to the existing shareholders provided such matter has been approved by the shareholders in a general meeting by way of a special resolution.

Now, the question arises, can the shareholders enter in to a consensual agreement providing issue of further shares to a particular class of shareholders / third party, since the decision pertaining to issue of further shares on preferential basis will be taken by the board of directors of the company and not by the shareholders? It is to be noted that there is no restriction under the CA 2013, which prevents the shareholders of a company to enter into a consensual agreement, therefore, the shareholders are free to enter into a consensual arrangement / contract stating that in case of issue of any further shares by the company, such further shares shall, in the first instance, be offered to the particular class of shareholders. However, such provisions shall be effective only on the compliance of the following conditions:

(i) Insertion of such provisions in AOA

Such provisions relating to further issue of shares are duly incorporated in the AoA of the company;

In Re: S.P. Jain Vs Kalinga Tubes Limited [(1965)1CompLJ 193 (SC)]

The shareholders of the company entered into an agreement with an outsider stating that any further issue of shares will be first offered to the said outsider. The said agreement was acted upon by the parties in few instances, as some shares were issued to the outsider. Subsequently, the said company was converted into a public company and thereafter, any further shares issued by the company were not offered to the said outsider. The said outsider filed a suit on the ground of oppression and mismanagement.

Hon'ble Supreme Court in the aforesaid matter held that neither was the company a party to the said agreement nor were the terms of such agreement incorporated in the AoA of the company, therefore, the company is not bound by the said agreement. The company acted in terms of its AoA and the CA 1956 and therefore, it was concluded that it is not a case of oppression and mismanagement.

(ii) Shareholders Resolution

The shareholders of the company passes a special resolution under Section 61(1)(c) of CA 2013, which is a statutory requirement, for issue of shares to a particular class of shareholder(s) of a company in preference to other shareholders.

(iii) Compliance with ICDR Regulations (Applicable only to listed entity)

The provisions of Securities and Exchange Board of India (Issue of Capital and Disclosures Requirements) 2009 ("**ICDR Regulations**"), in relation to preferential issue of securities are duly complied with in case of preferential issue of shares by a listed public company.

(iv) Company should be made as a Confirming Party

While entering into any consensual arrangement, the company should be a confirming party to such consensual arrangement entered into by and between the shareholders, since, the case of issue of new shares is distinct from that of transfer of shares, as in the former case it is the company which is to issue and further allot the new shares while in the latter case the company's role is limited only to the extent of recognizing the transferee as a new shareholder.

In view of the above, any pre-emption rights given to any shareholders under consensual arrangement / contract are not negative per se provided that all the compliances under the CA 2013 and the AoA of such company are duly made by a private company or a public company, as the case may be.

SEBI's position on Pre-emptive Rights

SEBI, vide notification bearing number LAD-NRO/GN/2013-14/26/6667 dated October 3, 2013, has permitted contracts containing pre-emption rights including right of first refusal, tag-along or drag-along rights contained in the shareholders' agreements or AoA of companies.

Previously, the Central Government, vide Notification No. S.O. 1490 dated June 27, 1961, specified that **contracts for pre-emption** or similar rights contained in the promotion or collaboration agreements or in the AoA of limited companies are contracts to which Securities Contracts (Regulation) Act, 1956 ("**SCRA**") shall not apply.

Call & Put Option

Meaning:

'**Call Option**' means a right but not an obligation provided to the investor or shareholder to buy the shares on a future date from other shareholder(s).

'**Put Option**' means a right but not an obligation provided to the investor or shareholder to sell the shares on a future date to other shareholder(s) or third party(s), as the case may be.

Options in Securities

Options in securities are more appropriately dealt in SCRA which applies to unlisted and listed public company [In Re: Bhagwati Developers Private Limited Vs. Peerless General Finance and Investment Company Limited and another [2013]179CompCas421(SC)]. Hence, it is imperative to discuss and analyze the relevant provisions of SCRA in this regard:

(i) The term 'options in securities' finds its origin in SCRA, Section 2(d) of SCRA provides that:

"(d) option in securities" means a contract for the purchase or sale of a right to buy or sell, or a right to buy and sell, securities in future, and includes a teji, a mandi, a teji mandi, a galli, a put, a call or a put and call in securities;"

(ii) Section 20 of SCRA, which has been omitted by the Securities Laws (Amendment) Act, 1995, w.e.f. 25-1-1995, inter-alia, mentioned that all options in securities after the commencement of SCRA shall be illegal. The reason for the removal of such a restriction was that the Government was considering the facilitation of trading in 'derivatives' at that time and subsequently, SEBI, vide the Securities Laws (Amendment) Act, 1999 (w. e. f. 22-2-2000), made inter-alia the following significant changes in SCRA:

a) Insertion of Section 2 (ac) in SCRA (i.e. definition of derivatives); and
b) Insertion of the provisions of Section 18A of SCRA, which inter-alia provides that contracts in derivative shall be legal and valid if such are (i) traded on a recognized stock exchange; (ii) settled on the clearing house of the recognized stock exchange, in accordance with the rules and by-laws of such stock exchange.

(iii) Subsequent to omission of Section 20 of SCRA, SEBI, vide notification no. s.o. 184(E) dated March 1, 2000, provided that:

"*...no person in the territory to which the said Act extends shall, save with the permission of the Board, enter into any contract for sale or purchase of securities other than such spot delivery contract or contract for cash or hand delivery or special delivery or contract in derivatives as is permissible under the said Act or SEBI Act, 1992 (15 of 1992)*."

(iv) Pursuant to the provisions of Section 2(d) and Section 18A of SCRA, any contract or agreement giving call and put option at future date was considered as a 'derivative contract' (forward contract) which can only be traded on the floor of a stock exchange. Since, such a contract was not recognised as an eligible future contract and was not qualified as a spot delivery contract or contract for cash or hand delivery or special delivery or contract in derivatives as is permissible under the SCRA or SEBI Act, 1992, therefore, permission of the SEBI was required to enter into such types of contracts due to restriction placed in SEBI notification dated March 1, 2000.

SEBI's Clarification in the matter of Vulcan Engineers Limited

Further, in a **letter dated May 23, 2011, issued by SEBI to Vulcan Engineers Limited (Vulcan) and D. H. Law Associates (DHLA) in response to the letter dated February 22, 2011, issued by the Vulan to SEBI seeking guidance of the SEBI, in terms of the provisions of SEBI (Informal Guidance) Scheme, 2003** ("**SEBI Letter**"), SEBI has clarified that call/put option would not qualify as a legal and valid derivative contract in terms of Section 18A of SCRA as it is exclusively entered into between two parties and is not a contract traded on stock exchanges or settled on the clearing house of the recognized stock exchange.

MCX Judgement

Hon'ble High Court of Bombay in MCX Stock Exchange Limited Vs. Securities Exchange Board of India & Ors. [2012(114)BomLR1002] dated march 14, 2012, has taken a contrary view and inter-alia held that:

"*...A concluded contract for the sale and purchase of shares comes into existence only when the promisee upon whom an option is conferred, exercises the option to sell the shares. Hence, an option to purchase or repurchase is regarded as being in the nature of a privilege."*

In V.Pechimuthu vs. Gowrammal, 22 Mrs.Justice Ruma Pal, speaking for a Bench of the Supreme Court explained the nature of an option or privilege thus:

"*A privilege has been defined as a particular and peculiar benefit or advantage enjoyed by a person, and a concession as a form of privilege. An option to purchase or repurchase has been held to be such a privilege or concession (See Shanmugam Pillai v. Annalakshmi, (AIR 1950 FC 38; K.Simrathmull v. Nanjalingiah Gowder, AIR 1963 SC 1182). This is because an option by its very nature is dependent entirely on the volition of the person granted the option. He may or may not exercise it. Its exercise cannot be compelled by the person granting the option.*"

In view of the aforesaid MCX judgement, once the option is exercised by any of the parties to the contract, a contract giving a call and put option will be considered as a derivative contract and shall require the permission of SEBI unless:

(i) Such a contract is executed as spot delivery contract or contract for cash or hand delivery or special delivery or contract in derivatives as is permissible under the SCRA or SEBI Act, 1992.

(ii) Such call and put options are mentioned in the promotion or collaboration agreements to which SCRA will not apply [Notification No. S.O. 1490 dated June 27, 1961].

The aforesaid clarification by SEBI was a setback for the foreign investors since they always prefer easy exit options in the consensual arrangement.

Notification dated October 03, 2013

In order to address the concern of the foreign investors and to promote the foreign direct investment / merger & acquisitions in India, SEBI, vide notification bearing no. No. LAD-NRO/GN/2013-14/26/6667 dated October 3, 2013, has permitted contracts containing an option for purchase or sale of securities subject to compliance of the following conditions:

(i) the title and ownership of the underlying securities are held continuously by the selling party to such a contract for a minimum period of one year from the date of entering into the contract;

(ii) the price or consideration payable for the sale or purchase of the underlying securities pursuant to exercise of any option contained therein, is in compliance with all the laws for the time being in force, as applicable; and

(iii) the contract has to be settled by way of actual delivery of the underlying securities.

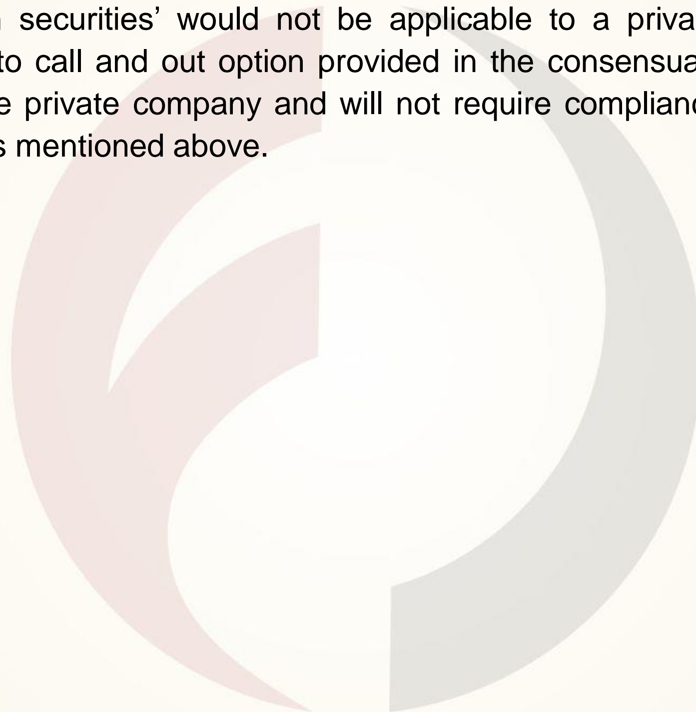
The contracts permitted under this notification shall be in accordance with the provisions of Foreign Exchange Management Act, 1999.

Further, this notification shall not affect or validate any contract which has been entered into prior to the date of this notification. Therefore, any consensual arrangement, in case of public company, providing call and out option(s) executed prior to the date of issuance of aforesaid notification, may come into the SEBI's scanner if the same qualifies as derivative contract.

The aforesaid notification supersedes the earlier SEBI notification i.e. S.O.184 (E) dated March 1,2000 which restricts any person to enter into any contract for sale or purchase of securities other than such spot delivery contract or contract for cash or hand delivery or special delivery or contract in derivatives as is permissible under the said Act or SEBI Act, 1992 (15 of 1992).

The aforesaid notification is also in line with the proviso to section 58(2) of the Companies Act, 2013 which states that “any contract or arrangement between two or more persons in respect of transfer of securities shall be enforceable as a contract".

It is to be noted that in case of a private limited company, the provisions of the SCRA will not apply since the shares of a private company are not considered as marketable securities which is one of the essential requirements to fall within the definition of ‘securities’ as mentioned in SCRA [Dahiben Umedbhai Patel and others Vs. Norman James Hamilton and others [1985]57CompCas700(Bom)]. Therefore, restrictions as provided under SCRA in relation to ‘option in securities’ would not be applicable to a private company and any provision pertaining to call and out option provided in the consensual arrangement will be legally binding on the private company and will not require compliance with the conditions stipulated by SEBI as mentioned above.



RBI's position on Pre-emptive Rights

The Reserve Bank of India ("**RBI**") does not restrict contracts for pre-emption rights. However, RBI, from time to time, has also objected on the equity instruments which has in-built option (call & put option) and assures definite return (IRR) or an option under the equity instruments, which takes away the equity characteristics of such instruments and safeguards the interest of a foreign shareholder from taking equity risk / capital risk in the venture / company then such instrument may be considered by the RBI as a debt instrument. Whether an equity instrument is debt instrument or not, it is a subjective issue and shall always be decided by the RBI on a case to case basis.

In a financial term, equity shares mean risk capital which confers on their holders the residue of rights of the company which have not been conferred on other classes. The equity shares usually carry the main financial risk if the company is unsuccessful, but they carry the greatest prospects of financial reward if the venture of the company is successful.

The return on equity instrument(s) by way of dividend is not a fixed return and depends upon the number of factors including profitability of a company etc. All the decisions pertaining to declaration of dividend are compulsorily required to be taken by the board of directors. After the approval of the board of directors of a company, such a decision will also need to be confirmed and approved of in a meeting of shareholders (generally annual general meeting).

Circular 2 of 2011

Earlier, the Government of India, by inserting the following clause 3.3.2.1 vide Circular 2 of 2011 (Consolidated FDI Policy), has de-classified instruments with options from being FDI investments:

"*3.3.2.1: Only equity shares, fully, compulsorily and mandatorily convertible debentures and fully, compulsorily and mandatorily convertible preference shares, **with no in-built options of any type**, would qualify as eligible instruments for FDI. Equity instruments issued / transferred to non-residents having in-built options or supported by options sold by third parties would lose their equity character and such instruments would have to comply with the extant ECB guidelines.*"

Subsequently, the Government of India, vide corrigendum to Circular 2 of 2011 (consolidated FDI policy) dated October 31, 2011, has deleted the aforesaid paragraph 3.3.2.1 from consolidated FDI policy issued vide Circular 2 of 2011. However, despite the removal of the aforesaid paragraph from Circular 2 of 2011, the RBI, while granting approvals to various foreign investors, has taken a view that any instrument which has in-built options for buy-back, put and call option with assured return is in the nature of a debt instrument for the reason that, in actual, there is no equity risk involved on the part of the foreign investor.

RBI Circular dated January 09, 2014

Finally, the RBI vide its circular dated January 9, 2014 [**A.P. (DIR Series) Circular No. 86**] has allowed the options in relation to equity shares and compulsorily and mandatorily convertible preference shares/debentures to be issued to a person resident outside of India under the Foreign Direct Investment (FDI) Scheme, subject to the following conditions:

(i) There is a minimum lock-in period of 1 (one) year or a minimum lock-in period as prescribed under FDI Regulations, whichever is higher (e.g. defence and construction development sector where the lock-in period of three years has been prescribed). The lock-in period shall
be effective from the date of allotment of such shares or convertible debentures or as prescribed for defence and construction development sectors, etc. in Annex B to Schedule 1 of Notification No. FEMA 2000 as amended from time to time;

(ii) After the lock-in period, as applicable above, the non-resident investor exercising option / right shall be eligible to exit without any assured return, as under:

(a) In case of a listed company, the non-resident investor, shall be eligible to exit at the market price prevailing at the recognised stock exchanges.

(b) In case of an unlisted company, the non-resident investor shall be eligible to exit from the investment in equity shares of the investee company at a price not exceeding that arrived at on the basis of Return on Equity ("**RoE**") as per the latest audited balance sheet. **Any agreement permitting return linked to equity as above shall not be treated as violation of FDI policy / FEMA Regulations**.

Note: For the above purpose, RoE shall mean Profit After Tax / Net Worth; Net Worth would include all free reserves and paid up capital.

(c) Investments in Compulsorily Convertible Debentures (CCDs) and Compulsorily Convertible Preference Shares (CCPS) of an investee company may be transferred at a price worked out as per any internationally accepted pricing methodology at the time of exit duly certified by a Chartered Accountant or a SEBI registered Merchant Banker. **The guiding principle would be that the non-resident investor is not guaranteed any assured exit price at the time of making such investment / agreement and shall exit at the price prevailing at the time of exit, subject to lock-in period requirement, as applicable**.

In view of the aforesaid Circular, the RBI has cleared its stand that any consensual arrangement in relation to any instrument which has in-built options for buy-back, put and call option with assured return is in the nature of debt instrument and shall not be allowed.

Earlier, the former RBI Governor '**Mr. Raghuram Rajan**' in a press conference dated February 3, 2014, said that:

"***These put-call options that were embedded in various investments. We have said we are not against them, we just want to make sure it is not hidden debt. So, if you have a put option but the put option is at a price which is lower than what you have invested. So you don't get a guaranteed debt return we are okay with that."***

"We are trying to make it easier for FDI. There are other features that were earlier not favoured, which we will open up as we look into this and come out with a detailed paper but the idea is to make it easier for FDI even with a variety of contractual features that would allow these investors to put money in."

In view of the above statement, it can be inferred that as long as 'equity instrument' does not contain the characteristics of 'debt instrument', the RBI may consider allowing the transactions pertaining to 'assured return' on a case to case basis.