

SEBI's new initiative: Listing of stock exchanges, green bonds' issuance & amendment to takeover code



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Introduction

1. SEBI, in its Board Meeting held on November 30, 2015, approved of certain new initiatives and amendment to its Regulations. Some key decisions include listing of stock exchanges, introduction of public consultation process for disclosure requirements for Green Bonds' issuance and listing, amendment to Takeover Code w.r.t. forfeiture of partly paid-up shares, exiting opportunity to dissenting shareholders (under the provisions of the Companies Act, 2013) and public issuance of convertible securities. The article provides analysis of the key decisions taken by the SEBI Board in its meeting, along with in-depth discussion on the concept papers floated after the board meeting.

2. Listing of the stock exchanges

2.1 Summary of the Decision: SEBI Board acknowledged the representations received from stock exchanges & market participants for listing and, accordingly, approved of the proposal by placing certain safeguards as provided in the Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporations) Regulations, 2012 ('SECC Regulations'). The Board approved of the listing of the stock exchanges subject to following conditions:

- (i) Maintaining of 51% shareholding of 'Public Category' and ensuring that holding of trading members/associates/agents does not exceed 49%. It has suggested mechanism to be put in place for approval of listed stock exchange as and when holding of trading members/associates/agents reaches 45%. The definition of 'associate' is proposed to be amended;
- (ii) For ensuring compliance that every shareholder be 'fit & proper', each applicant is under an obligation for making such declaration at the time of making application during IPO/OFS;

- (iii) Shareholding threshold of 2%, 5% or 15%, as the case may be, shall be monitored through Depository mechanism;
- (iv) Stock Exchanges shall be classified as 'infrastructure cos.' under the SEBI (ICDR) Regulations, 2009.

2.2 Analysis of the Decision: In June 2012, based on Bimal Jalan Committee's recommendations, the SEBI allowed stock exchanges (more than 3-years old) to list their own shares through an IPO based on certain guidelines, however, certain clauses in the existing SECC Regulations were acting as barriers for such listing. The stock exchange listing will provide an exiting opportunity to shareholders, improve corporate governance and disclosures towards the stakeholders. It is noteworthy that BSE Ltd. had filed draft Red Herring Prospectus with the SEBI more than 3-years ago, but the approval is still awaited. Now, on compliance of prescribed conditions by BSE, many of its shareholders can now cash-in and exit from the exchange.

3. 'Green Bonds' - Issuance & listing

3.1 Summary of the Decision: The SEBI Board considered and approved of the proposal for initiation of public consultation process for disclosure requirements for issuance and listing of Green Bonds. The Board noted that such Green Bonds are in line with the requirements as provided for in 'Green Bond Principles' as recommended by International Capital Market Association. It was also noted that the issuance and listing of Green Bonds in India does not require any amendment to the SEBI (Issue and Listing of Debt Securities) Regulations, 2008 and the issue, listing and disclosure requirements as prescribed under the said Regulations will continue to be applicable. SEBI has also floated concept paper on 'Green Bonds'.

3.2 Analysis of the Decision & Concept Paper: Green Bond is just like any other debt instrument issued for raising funds from

investors. However, the proceeds from such issue are earmarked for use towards financing 'green projects'. The key difference between Green Bond and regular bond is that the issuer-company states that it is raising capital to fund 'green' projects, assets or business activities with an environmental benefit, such as renewable energy, low carbon transport, etc. Green Bonds can help in enhancing the issuer company's reputation, as this is an effective way of demonstrating its green credentials. It also shows the issuer company's commitment towards development and sustainability of the environment. Since the capital is earmarked for investment in green projects, it provides the issuing company an access to such investors which they otherwise may not be able to tap with a regular bond. Issuance of Green Bonds attracts wider investors' base, which may benefit the issuer company in better pricing. Further, with increasing focus of the global investor community towards green investments, it is expected that new set of investors will enter into this space leading to lowering of the cost of funding for green projects.

4. Amendment to takeover code

4.1 Summary of the Decision: SEBI Board has also approved of the proposal of amending Takeover Code, 2011 for providing general exemption from open offer obligations arising due to 'passive increase' in voting rights as a result of expiry of call notice period and forfeiture of shares. The SEBI has floated a concept paper on the amendment to Takeover Code.

4.2 Analysis of the Decision & Concept Paper: SEBI has suggested that increase in shareholding due to expiry of call notice period and forfeiture of shares may be treated as a 'passive acquisition', for the reasons: (i) Accrual of voting rights to the remaining shareholders, computed on *pro rata* basis, upon the expiry of call notice issued to the shareholders holding partly

paid-up shares is also passive in nature, (ii) Forfeiture is undertaken in accordance with the Companies Act, 2013 where it is at full liberty to undertake this to remove defaulting shareholders from Members' Register.

With respect to 'incidental increase' in voting rights without a positive act of an acquirer, SAT [in the case of *Raghu Hari Dalmia v. SEBI* [2011] 16 taxmann.com 100/110 SCL 634 (Mum. - SAT)] had ruled that increase in voting rights of appellants was not by reason of any act of theirs, but was incidental to the buyback of shares of other shareholders by the company and such a passive increase in the proportion of their voting rights would not attract Regulation 11(1) of the SEBI Takeover Code, 1997. In a recent SEBI ruling in *Emmons International Ltd.*, SEBI held that share forfeiture is not a 'passive acquisition' like buyback of shares, since forfeiture of shares is orchestrated by the management/promoters of the company and can be made only by the Board of Directors by passing a resolution. The management/promoters are very well aware of the forfeiture proceedings, since they have access to the records of the company.

SEBI observed that such an exercise for 'passive' activity would take enormous amount of time and effort. Accordingly, SEBI has proposed to amend the Takeover Regulations, 2011 by providing general exemption from open offer obligations in cases of increase in voting rights as a result of the expiry of call notice period and the forfeiture of shares in line with general exemptions available with respect to rights issues, buybacks, etc.

5. Primary market debt offering through private placement on e-book

5.1 Summary of the Decision: SEBI Board considered and approved of the proposal for initiation of public consultation process on introduction of "Primary Market Debt Offering through private placement on electronic Book".

5.2 Analysis of the Decision & Concept Paper:

The key benefits of such an electronic platform, *inter alia*, are improvement in efficiency and transparency of the price discovery mechanism *vis-à-vis* the extant over-the-telephone market coupled with possible reduction of cost and time taken for such issuances. SEBI has observed that usage of electronic book by investors for trading in securities in the Indian markets have demonstrated that the benefits can arise in terms of efficient price discovery, reduction in timelines, reduction of cost, transparency, etc. It is proposed that such an electronic book may be created by entities to be named as 'Electronic Book Providers' (EBPs). The entities such as stock exchanges, depositories and Merchant Bankers with net worth above ₹100 crore may apply to SEBI for setting-up EBPs. Concept Paper on "Primary Market Debt Offering through private placement on electronic Book" has also been floated for public comments.

6. Deemed public issues

6.1 Summary of the Decision: SEBI noted that after effective date of the Companies Act, 2013 (*i.e.*, on or after April 1, 2014), any offer or allotment of securities shall be considered as 'public issue' if the number of offerees/allottees exceeds 200 persons in a financial year (under the Companies Act, 2013) as against the cap of 49 persons (under the Companies Act, 1956). SEBI Board approved that in respect of the cases involving issuance of securities to more than 49 persons but up to 200 persons in a financial year, the companies may avoid penal action if they had provided investors with an option of surrendering securities and get refund amount at a price not less than amount of subscription money paid along with 15% interest p.a. thereon. However, such exiting is subject to certain conditions.

6.2 Analysis of the Decision: It is proposed that exiting may be provided by: (i) Company, or (ii) Promoters or (iii) Such persons as are

arranged by the company/promoters, whereby the companies may adjust the amounts already paid to the allottees either as interest/dividend or otherwise from the amount of refund to be paid to the investors. With an objective of monitoring the refund process and having an independent check, the process would be certified by independent Practicing CA/Practicing CS/Practicing Cost Accountants. The SEBI decision aims to harmonise the provisions of the Companies Act, 2013 and Companies Act, 1956, and at the same time protects the company from penal action, if the securities are issued to more than 49 persons and less than 200 persons. However, it is noteworthy that there is reference of the phrase 'surrender of securities', and presently there is no detailed provision and procedure in the Companies Act and SEBI Act for such surrender, and, therefore, the implementation of such provision is the key to the effectiveness of SEBI's decision.

7. Exiting opportunity to dissenting shareholders

7.1 Summary of the Decision: The SEBI Board approved of the proposal to initiate public consultation process regarding exiting opportunity to dissenting shareholders under the Companies Act, 2013 in case of change in objects or varying the term of contracts referred to in the prospectus. In this regard SEBI has floated a concept paper on exiting opportunities to dissenting shareholders.

7.2 Analysis of the Decision & Concept Paper: The Discussion Paper issued by the SEBI relates to section 13(8) and section 27 of the Companies Act, 2013. Section 13(8) of the Companies Act, 2013 (relating to 'alteration of memorandum') states that company, which has raised money from public through prospectus and still has any unutilised amount out of the money so raised, shall not change its objects for which it raised the money through prospectus unless a special resolution is passed

by the company and dissenting shareholders are given an opportunity to exit by the promoters and shareholders having control in accordance with the SEBI regulations. Section 27 of the Companies Act, 2013 (relating to 'Variation in terms of contract or objects in prospectus') states that a company shall not, at any time, vary the terms of a contract referred to in the prospectus or objects for which the prospectus was issued, except subject to the approval of, or subject to an authority given by the company in general meeting by way of special resolution and the dissenting shareholders (being those shareholders who have not agreed to the proposal to vary the terms of contracts or objects referred to in the prospectus), shall be given an exiting offer by promoters or controlling shareholders at such exit price, and in such manner and conditions as may be specified by the SEBI.

SEBI states that investors in secondary market take an informed investing decision in company's equity shares after doing the necessary background check, i.e., understanding the company's objects for which money has been raised. Therefore, such investors should also be given a fair opportunity of exiting, where they do not agree to change the object. SEBI states that suitable changes in the Companies Act, 2013 are required, where exit offer is to be given where there are no identifiable promoters or shareholders having control can be exempted from such requirement. SEBI states that suitable changes in the Companies Act, 2013 are required, where company has already utilized higher percentage of the amount raised and intends to change the objects to some extent due to certain reasons.

8. Public issuance of convertible securities

8.1 Summary of the Decision: The SEBI Board approved of the proposal to initiate public consultation process for revival of public issuance of convertible securities by

listed entities, for which Concept Paper has been floated.

8.2 Analysis of the Decision & Concept Paper:

Convertible security offers unique combination of debt and equity to investors. Holder of such security can convert it into equity and benefit, if the issuer-company performs well. However, if the issuer-company is not performing as per expectations, security holder has the option of redeeming it at a pre-determined maturity date. Issuing convertible securities helps the company to secure equity financing in a delayed manner, whereby dilution process of common stock and earnings per share is delayed. Based on the market participants' representations, with a view of reviving issuances of convertible securities and providing additional investment avenue for investors, SEBI proposes to review framework for public issuance of convertible securities.

SEBI proposes that the tenure of convertible securities issued to public by an existing listed entity may be of 5 years maximum. (Presently, there is no specific provision for tenure of convertible securities issued to public, except for financing of a group company where the maximum tenure can be 18 months). SEBI also proposes that the conversion price may either be pre-fixed at the time of issue or linked to market price at the time of conversion, with necessary disclosures in the offer document. (Presently, whether an issuance can be made on a fixed price basis or through the book building route depends on meeting of specified eligibility criteria). SEBI also proposes to explicitly permit existing holders of convertible securities to sell their securities to public. (Currently, while the existing shareholders are permitted to sell their shares to public, the same is not specifically mentioned for convertible securities)

9. Delisting of small companies

9.1 Summary & Analysis of the Decision:

Presently, the SEBI Delisting Regulations

provide for a simplified delisting procedure for small companies and exempt them from the requirements of Chapter IV of the Delisting Regulations subject to certain conditions. Based on the suggestions received from Investor Association, SEBI Board has approved of the proposal that condition of no trading for preceding 1 year may be relaxed and the small companies, whose trading of equity shares during the 12 calendar months is less than 10% of the total number of shares of such company, would also be eligible for simplified procedure of delisting. However, to protect the investors' interest, the exit price shall not be less than floor price determined for the purpose of Reverse Book Building for not frequently traded securities in terms of the Delisting Regulations, read with the SEBI Takeover Regulations.

10. Business responsibility reporting

10.1 Summary & Analysis of the Decision:

SEBI Board has extended the applicability of Business Responsibility Reporting ('BRR') to top 500 listed entities based on market capitalization as on March 31st of every year. BRR can be displayed on the websites of the companies providing website link for the same in their annual reports. As per clause (f) of sub-regulation (2) of regulation 34 of the Listing Regulations, the annual report shall contain a BRR describing the initiatives taken by the listed entity from an environmental, social and governance perspective. SEBI Circular¹ has prescribed the format for BRR.

Conclusion

11. SEBI's approval to the proposal of listing of Stock Exchanges has been one of the most awaited decisions. It will be interesting to see the implementation of entire process alongwith the compliance of certain safeguards and governance norms as provided for in the Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporations) Regulations, 2012.

SEBI's other decisions also include introduction of public consultation process for disclosure requirements for Green Bonds' issuance and listing, public issuance of convertible securities will result in depth in the securities market and also provide investors with a different

investment avenue. SEBI's decision relating to amendment to Takeover Code w.r.t. forfeiture of partly paid-up shares, exiting opportunity to dissenting shareholders will assist the corporates in decisions relating to corporate restructuring.

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1. *Vide* SEBI Circular No. CIR/CFD/CMD/10/2015, dated November 4, 2015.