

M&A Hotline

November 25, 2014

THE BIG BANG OF THE INDIAN CAPITAL MARKET

- SEBI (Prohibition of Insider Trading) Regulations, 2014 introduced;
- SEBI (Delisting of Equity Shares) Regulations, 2009 amended;
- Listing Agreement converted into SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2014

In its continual efforts to revamp the existing market regulatory framework, Securities and Exchange Board of India ("SEBI") in its **board meeting** held on November 19, 2014 ("**Board Meeting**") has finally cleared three of the much awaited big ticket regulations. While we await notification of these regulations, Nishith Desai Associates brings you this alert to provide a brief overview of some of the key decisions taken in the Board Meeting.

I. INTRODUCTION OF SEBI (PROHIBITION OF INSIDER TRADING) REGULATIONS, 2014 ("2014 PIT REGULATIONS")

The 22 years old SEBI (Prohibition of Insider Trading) Regulations, 1992 ("**1992 PIT Regulations**") has finally been replaced with the SEBI (Prohibition of Insider Trading) Regulations, 2014 in light of the recommendations made by an 18 member committee ("**Committee**") constituted by SEBI under the chairmanship of Justice N.K. Sodhi, former Chief Justice of the High Courts of Kerala and Karnataka. Please see our hotline on the Committee recommendations [here](#). SEBI in its Board Meeting has highlighted the following key changes in the forthcoming 2014 PIT Regulations:

KEY CHANGES

'Insider'

The definition of 'insider' has been made wider by including persons connected on the basis of being in any contractual, fiduciary or employment relationship that allows such person access to 'unpublished price sensitive information' ("**UPSI**"). Immediate relatives are also deemed to be insiders with an ability to rebut such a presumption. In case of connected persons, the onus of establishing, that they were not in possession of UPSI shall lie on such connected persons.

'Unpublished Price Sensitive Information'

UPSI has been defined as information not generally available and which may impact the price. The definition of UPSI has been strengthened by providing a test to identify price sensitive information, aligning it with listing agreement and providing platform of disclosure. Earlier, the definition of price sensitive information had reference to company only; now it has reference to both a company and securities. Generally available information will be the information that is accessible to the public on a non-discriminatory platform which would ordinarily be stock exchange platform.

Communication and procurement of UPSI now prohibited

The 2014 PIT Regulations also prohibit the act of procuring UPSI.

Facilitating Legitimate Business Transactions

The requirement of communication of UPSI in the case of legitimate business transaction has been recognized in law and a carve-out with safeguards has been provided. Accordingly, to facilitate legitimate business transactions, UPSI can be communicated with safeguards.

Trading Plans

In line with the concept of 'pre-arranged trading plans' prevalent in the United States, the 2014 PIT Regulations have now introduced the safe harbour provision of trading plans by virtue of which an 'insider' who is liable to possess UPSI round the year may deal with securities in pursuance of trading plans formulated and disclosed on stock exchange platform in advance, with appropriate safeguards.

Disclosures

Considering every investor's interest in securities market, advance disclosure of UPSI at least 2 days prior to trading has been made mandatory in case of permitted communication of UPSI.

Valid Defences

The 2014 PIT Regulations also provide for valid defences i.e. certain circumstances which can be demonstrated by an insider to prove his innocence.

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Since, the Takeover Regulations already prescribe relevant disclosures, persons holding more than 5 % shares or voting rights in a listed company are not required to make repeated disclosures under the 2014 PIT Regulations in case of change of every 2 % in its shareholding or voting rights. Section 194 of the Companies Act which prohibits derivative trading by directors and key managerial personnel on securities has been specifically incorporated in the 2014 PIT Regulations.

Quick Takeaways

- The scope of the term ‘insider’ has been broadened. While this is *prima facie* a positive step intended to bring more people within the ambit of the term, such wide definition should not impede operations of the company or performance of professional obligations. It is not clear from the minutes of the Board Meeting if the wide definition of the term ‘insider’ is qualified by certain exceptions and defences that could strike a balance between the interests of the public shareholders and the business requirements of the company.
- The uncertainty under the 1992 PIT Regulations with respect to disclosure of UPSI for the purposes of genuine M&A and PE transactions has been a constant source of concern for India Inc. and foreign investors. The demand for permission to share UPSI in PE/ M&A backed diligences seems to have been accepted finally. The carve out for facilitating legitimate transactions with safeguards is a huge step towards progress of Indian capital markets.

II. SEBI (DELISTING OF EQUITY SHARES) REGULATIONS, 2009 (“DELISTING REGULATIONS”)

SEBI had released a [discussion paper](#) in May, 2014 on ‘Review of the Delisting Regulations’, after consultation with various market participants and investor associations to safeguard the interest of investors. SEBI has now broadly approved the following amendments to the Delisting Regulations (“**Delisting Amendments**”):

Threshold Limit

SEBI has streamlined the threshold limit for a delisting offer to be successful. As per the Amendment, once post offer, the shareholding of the promoter/acquirer reaches ninety per cent of the total issued capital **and** at least twenty five per cent of the number of public shareholders tender in the reverse book building process, the offer is deemed successful.

Price Discovery

SEBI has modified the price discovery process under the Delisting Regulations. As per the amendment, the offer price determined through Reverse Book Building shall be the price at which the shareholding of the promoter, after including the shareholding of the public shareholders who have tendered their shares, reaches the threshold limit of 90%.

Restrictions on Delisting

To further ensure the acquirers do not side-step the price discovery mechanism, SEBI has introduced a new restriction for making a delisting proposal. The Amendment provides that the promoter/promoter group is prohibited from making a delisting offer in case any entity belonging to the same group has sold shares of the company during a period of six months prior to the date of the board meeting which approves the delisting proposal.

Platform

SEBI has approved use of stock exchange platform for offers made under Delisting, SEBI (Buy back of Securities) Regulations, 1998 and Takeover Regulations.

Timeline for Completion

SEBI has indicated that the timeline for completion of the delisting process has been reduced to only 76 working days from 137 calendar days (approx 117 working days).

Onus on the Board of Directors

The Delisting Amendments cast an obligation on the Board of Directors of the Company to ensure that the delisting proposal is approved only if it is in the interest of the shareholders and that the company is in compliance with all the applicable securities laws. The Board of the company is further required to appoint a Merchant Banker for compliances under the Delisting Regulations.

Small Companies and Delisting

The Delisting Amendment has raised the threshold limit for ‘small companies’ so as to exclude all companies with paid up share capital less than INR 10 crores and net worth less than INR 25 crores from following the Reverse Book Building (“**RBB**”) process provided that there is no trading activity during one year prior to the board meeting approving the delisting proposal and trading of the shares of the company were not suspended for any non-compliance during such period.

Delisting directly pursuant to Open Offer

SEBI has now allowed the acquirer to delist shares of the company directly pursuant to an open offer in case the post-acquisition shareholding of the promoter crosses the threshold limit provided under the Delisting Regulations. It must be noted that in case the delisting attempt fails, the acquirer would be required to complete the mandatory open offer process under the Takeover Regulations and pay interest at the rate of 10% p.a. for the delayed open offer.

Harmonizing Delisting Amendments with the existing regulatory framework

One of the other amendments that have been introduced is that SEBI, for reasons recorded in writing, may relax or exempt strict compliance of any requirements under the Delisting Regulations, in line with the provisions existing in ICDR and Takeover Regulations.

Quick takeaways

Not many open offers in India have been successful in the recent past. One of the biggest contributors to the failure of the open offers have been the fact that open offers have been treated as off-market transactions and the consequent tax disadvantages. Now, use of stock exchange platform for delistings, open offers and buy-back has now been approved by SEBI. India Inc. should witness more successful open offers and delistings now.

Since, the Takeover Code allowed parties to seek exemption from compliances with the provisions of the Takeover Code, there was a natural urge to seek exemption from certain compliances under the Delisting Regulations especially because many Indian promoters faced practical difficulties in adhering to the technicalities of the Delisting Regulations. However, there was no express provision under the SEBI Delisting Regulations for seeking such exemption like the Takeover Code. Therefore, the move to permit seeking exemptions from meeting the requirements under the Delisting Regulations is commendable and could lead to more delistings though at the cost of increasing SEBI's work load.

III. INTRODUCTION OF SEBI (LISTING OBLIGATIONS AND DISCLOSURE REQUIREMENTS) REGULATIONS, 2014 ("LISTING REGULATIONS").

In order to enhance the enforceability of Listing Agreements, SEBI in the Board Meeting also approved the Listing Regulations which provide for a comprehensive framework governing various types of listed securities thereby replacing the extant Listing Agreements. The Securities Contract (Regulations) Act, 1956 mandatorily requires every person whose securities are listed on a stock exchange to comply with the conditions of the listing agreement with that stock exchange, which essentially provides for the initial and continual disclosure norms for such persons. In May 2014, SEBI had released its **approach paper** on draft SEBI Listing Regulations.

The Listing Regulations have been sub-divided into three parts i.e. (a) the main body of Regulations provides for substantive provisions (b) Schedules to the Regulations provide for procedural requirements (c) Circulars by SEBI which would prescribe for the forms of disclosures. More importantly, most of the provisions of the Listing Regulations have been well aligned with the provisions of the Companies Act, 2013.

SEBI has introduced overarching common obligations with respect to filing of information, responsibilities of compliance officer, fees etc. applicable to all types of listed securities and also, provided for specific obligations for each type of securities. SEBI has further indicated in the Board Meeting that a shortened version of the Listing Agreement within six months of notification of the Listing Regulations is necessary.

KEY PROVISIONS

Principles governing disclosures and obligations

A chapter has been included in the beginning of the Listing Regulations, governing disclosures and obligations of all listed entities. These principles are broadly in line with the International Organization of Securities Commissions (IOSCO) Principles for periodic disclosures by listed entities.

Corporate Governance

SEBI had already issued a revised Corporate Governance Framework vide its **Circular** dated April 17, 2014 which came into effect from October 01, 2014, which has been now included in the Listing Regulations as well.

Filing of Information

Filing on stock exchanges through electronic platform has been made mandatory, in order to promote electronic filing through technologically updated platform

Compliance Officer

The Listing Regulations provide for mandatory appointment of Company Secretary as compliance officer except for units of Mutual Funds listed on Stock Exchanges.

Registration with SEBI SCORES

All listed companies are required to register with SEBI SCORES in order to handle investor complaints electronically. This **requirement** introduced by SEBI in August 2014 has now been incorporated in the Listing Regulations.

Co-operation with Intermediaries

In order to enable registered intermediaries fulfil their obligations under the Listing Regulations, co-operation with such intermediaries has been made mandatory for all listed companies.

Annual Information Memorandum

An enabling provision for all listed entities to submit to the Stock Exchange Annual Information Memorandum as specified by SEBI from time to time has been incorporated in the Listing Regulations.

Small and Medium Enterprises

Various provisions of the equity listing agreement have now been extended to SMEs, in order to ensure uniformity in the disclosure requirements.

Provisions of Equity Listing Agreement also applicable to NCRPS and NCDS

Certain provisions of the equity listing agreement such as submission of Form B (audit reports), transfer and transmission of securities etc., which were earlier not applicable to NCRPS and NCDS, have also now been made applicable.

Quick Takeaways

o Replacement of Listing Agreement with Listing Regulations now provide for a more consolidated framework for the disclosures to be made by all listed entities and give statutory recognition to the listing norms in India.

IV. OTHER AMENDMENTS

- The FVCI Regulations till now did not allow investments in NBFCs except Equipment Leasing and Hire Purchase

- Companies. To encourage investments in infrastructure, the Board approved amendments in FVCI Regulations to allow FVCIs to invest in NBFC-CIC (Core Investment Companies), as defined by RBI.
- SEBI has approved a proposal permitting AMCs who are yet to meet with the revised net worth requirement of INR 50 crore, to launch a maximum of two schemes per year till the time such AMCs meet with the net worth requirements. Such permission would be considered on a case to case basis, depending on such AMCs demonstrating that serious efforts are being made by them to meet the net worth requirements within the prescribed timelines.
 - In case of minor violations, SEBI has decided that prior to an enforcement action being initiated against a party and before issuance of a show cause notice, an intimation would be sent to the concerned party. This provision shall now enable the concerned parties to seek settlement or make voluntary submissions beforehand.
 - SEBI has also now initiated public consultation process on 'Reclassification of Promoters as Public Shareholders and 'Issuance of partly paid shares and warrants by Indian companies'.

CONCLUSION

The aforementioned Regulations approved by SEBI are expected to be notified in the near future, while we note that some of the reforms introduced by SEBI are in line with the committee reports and discussion/approach papers earlier released by SEBI, we are yet to evaluate in detail nuances of these reforms. In its endeavour to provide clearer and stricter market regulatory framework, these changes introduced by SEBI are aimed to protect and safeguard the interest of investors, boost the market participation in India and more importantly, bring the Indian capital market at par with the global standards. We will provide a detailed analysis of these Regulations once the Regulations are notified.

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