Women Entrepreneurs vs. Housewives

The Securities Appellate Tribunal, in an appeal filed by DLF Limited and its officers, was divided on the validity of the SEBI order wherein, DLF was found to have made misrepresentations in its prospectus by not including necessary disclosures regarding Sudipti Estates Private Limited (such as details pertaining to an FIR filed against Sudipti). The primary issues were: (i) whether Sudipti was a subsidiary of DLF; and (ii) whether DLF's failure to make the necessary disclosures pertaining to Sudipti during its IPO amounted to violations of the SEBI (DIP) Guidelines, 2000 and the SEBI (PFUTP) Regulations, 2003. While DLF took the stand that it had disposed its shareholding in Sudipti to independent investors prior to the IPO, the Whole Time Member observed that these transfers were sham transactions as the new shareholders were the wives of certain key management personnel of DLF and that DLF continued to control Sudipti.

During the appeal, two members of SAT constituting the majority, observed that the new shareholders of Sudipti, being women entrepreneurs, were legitimate shareholders of Sudipti, and that there was no evidence to show that DLF continued to exercise control. Accordingly, they held that the transfer of shareholding was not a sham and that the WTM's order was *entirely unsustainable* and amounted to over-regulation. However, the Presiding Officer who constituted the minority, relying on an affidavit filed by the new shareholders stating that they were not involved in running the subsidiary, held that, DLF continued to exercise control over Sudipti as the transfers undertaken to the housewives of KMPs of DLF were sham transactions. Nevertheless, in light of certain mitigating factors in favour of DLF, he held the WTM order to be *partially unsustainable.* Owing to the conflicting views of SAT, it is likely that SEBI will prefer an appeal to the Supreme Court for a final pronouncement.

SEBI Guidelines for International Financial Services Centre

Consequent to the announcement in the Union Budget 2015 to set up an International Finance Services Centre (IFSC) in Gujarat International Finance Tec-City (GIFT City), SEBI passed the SEBI (International Financial Services Centres) Guidelines, 2015, on 27 March, 2015, to be made effective from 1 April, 2015. IFSC is meant to create a vibrant financial environment on the lines of finance centres in Singapore and Dubai. This would help capture billions of dollars worth of financial services that currently go to locations outside India, such as currency and bond derivative trading.

The Guidelines seek to regulate financial services relating to securities market in the IFSC created under Section 18(1) of the Special Economic Zones Act, 2005. The Guidelines allow domestic and foreign entities to undertake a variety of activities relating to securities market in the IFSC, subject to SEBI's approval. Any Indian recognised stock exchange or stock exchange of a foreign jurisdiction may set up a subsidiary, wherein it holds atleast 51% of the paid-up equity share capital, to carry on activities of a stock exchange in the IFSC. Further, a stock exchange can be set up with Rs. 25 crore capital, as against the normal requirement of Rs. 100 crore (though this will have to be raised to Rs. 100 crore within 3 years). Similar provisions have been made in relation to clearing corporation sand depositories. Further, stock exchanges can also set up clearing corporations in the IFSC.

Further, all entities in the IFSC would have to comply with IOSCO principles, principles of Financial Market Infrastructures (FMIs) and the governance norms as specified by SEBI. The Guidelines provide for dealing in equity shares of a company incorporated outside India, depository receipts, debt securities, currency and interest rate derivatives and index based derivatives. Domestic companies intending to raise capital in the IFSC in a currency other than Indian Rupee shall be subject to the Foreign Currency Depository Receipts Scheme, 2014 and foreign companies intending to raise capital shall have to comply with the provisions of the Companies Act, 2013 and the SEBI (ICDR) Regulations, 2009.

The Guidelines clearly indicate that the entities operating in the IFSC will be governed by the overall framework of securities regulations, with certain carve outs as specified in the Guidelines. This would help set up market infrastructure in such centres with relative ease and lead to greater capital market activities. However, for this important venture to succeed there has to be clarity on issues relating to taxation of these entities operating in the financial special economic zones, along with close coordination between the Government of India, RBI and SEBI.

Debt to Equity Conversion Norms Relaxed

SEBI, in its Board Meeting dated 22 March, 2015 approved a proposal to ease the process of debt to equity conversion for lending institutions in cases where their listed borrower companies are in distress. SEBI seeks to exempt such conversions from the applicability of certain provisions under the SEBI (ICDR) Regulations, 2009 and the SEBI (SAST) Regulations, 2011. This would be done by diluting the pricing guidelines. Currently, the minimum conversion price has to be the higher of the 26-week or the 2-week volume weighted average price of the stock from the relevant date. A minimum conversion price for a company in distress, discouraged lenders from taking up equity as there was a fear of further erosion of capital with a subsequent fall in the share price. As per the new norms, conversion would happen at a *"fair price"* not being less than the face value of the shares. This change was necessary. However, a minimum floor price of par value may act as a dampener for many highly distressed situations.

SEBI's decision is well-intended to revive distressed listed companies and provide more flexibility to the lending institutions to acquire control over the companies in the process of restructuring. It would benefit lenders and borrowers alike. Total NPAs for banks as on December 2014 was close to Rs. 3,00,000 crores. Easier conversion norms will not only help banks, especially public sector banks to clean up NPAs, but also reduce interest burdens for companies in distress. Although, the formal notification is awaited, the conversion price would now primarily be decided as per the negotiations between the lender and the borrower. Concerns regarding further litigation on grounds of unequal bargaining power in such negotiations cannot be ruled out. Further, an open offer exemption under the SEBI (SAST) Regulations, 2011 is expected and this would substantially lower the cost of conversion for banks.

Although this change would tempt banks to convert, certain concerns cannot be ignored - Can conversion ensure the revival of a company? How far can banks walk in the shoes of a promoter / substantial shareholder? Would banks have the requisite skill to participate in the management of a company? What happens to the management when the banks want to exit?

Issue of Debt Securities by Municipalities

SEBI, in its Board Meeting dated 22 March, 2015 approved the SEBI (Issue and Listing of Debt Securities by Municipality) Regulations, 2015, thereby providing a regulatory structure for public issuance of debt securities, and listing of debt securities issued through public issue or privately placed bonds by Municipalities. A Municipality is a self-government institution constituted under Article 243Q of the Constitution (Seventy-fourth Amendment) Act, 1992 and includes a Municipal Corporation, a Municipal Council, and a Nagar Panchayat. Municipalities can issue 'general obligation bonds' wherein the Municipality would pay the amount through its taxation power, and 'revenue bonds' which are serviced by project revenues. General bonds shall be issued only on a private placement basis, while revenue bonds can be issued through public offering or private placement. Safeguards have been prescribed to protect investors, such as the Municipality should not have a negative net worth in any of the last three preceding financial years and should have an investment grade rating. Further the Municipality should not have defaulted in repayment of debt securities or loans obtained from Banks / Financial Institutions, during the previous 365 days.

Further, the funds raised can be used only for the projects that have been specified in the offer document. They shall have a separate escrow account for servicing them with the earmarked revenue from the projects. Moreover, Banks / Financial Institutions will be appointed as monetary agencies which will make periodic reports. The appointment of such monitoring agencies will help keep the public and investors updated on a timely basis as to how the bonds are being serviced and will help to ensure compliance. The proposed regulations provide a clear mechanism for undertaking the issuance of municipal bonds and may play an important role in improving the regulatory conditions that presently hinder such issuances. These proposed regulations for municipal bodies to raise money from the market will attract large institutional investors and pave way for municipal bonds for infrastructure projects in urban areas. However, unlike government securities, these are not risk free bonds and therefore may not be suited for retail or unsophisticated participants who may assume them to be risk free.

Review of Continuous Disclosure Requirements for Listed Entities

SEBI, in its Board Meeting dated 22 March, 2015 approved certain changes to the proposed SEBI (Listing Obligations and Disclosure Requirements) Regulations, after having reviewed the requirements relating to disclosures being made by listed entities on a continuous basis. Some of the key changes are as follows. A listed entity will have to disclose all events / information, first to stock exchange(s), not later than 24 hours of occurrence of event / information. Similarly, the outcome of board meetings shall be disclosed within 30 minutes of the closure of the meeting of Board of Directors. Further, the listed entity needs to disclose all events / information with respect to its material subsidiaries. The existing list of events shall be rationalized into two parts: events which are by nature material i.e., those that necessarily require disclosure without any discretion by the listed entity; and events which shall be treated to be material as per the guidelines for materiality, as specified by SEBI. SEBI would specify an indicative list of information which may be disclosed upon occurrence of an event. Furthermore, the listed entity shall provide specific and adequate reply to queries of stock exchange(s) pertaining to rumours.

SEBI has sought to control the existing level of discretion given to listed companies to decide on the materiality of events, since it resulted in inadequate disclosures. In a measure to strictly monitor compliance with disclosure or listing norms, SEBI seeks to convert the same into regulations, where by non-compliance will be met by strong penal action. While the move aims to help investors make well-informed investment decisions, it may result in a lot of unnecessary information being disclosed in the public domain. Further, companies may find it difficult to ascertain within a day whether an event / information is required to be disclosed under the vague tests of materiality proposed to be introduced by SEBI. It should be clarified that merely because certain information is material, it does not mandate disclosure. Such a requirement would give away a lot of the competitive advantage and intellectual property of a company.

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