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Analysing developments impacting business

SEBI INTRODUCES NEW GUIDELINES FOR THE PREFERENTIAL ISSUE AND INSTITUTIONAL PLACEMENT OF UNITS BY INVITs

11 December 2019 **Background**

India's capital markets regulator, the Securities and Exchange Board of India (SEBI), has on 27 November 2019 introduced the "*Guidelines for the Preferential Issue of Units and Institutional Placement of Units by a listed Infrastructure Investment Trust*" (2019 Guidelines), applicable to listed infrastructure investment trusts registered with SEBI (InvITs). With a view to further simplify fund raising methods, the 2019 Guidelines have repealed the "*Guidelines for Preferential Issue of Units by Infrastructure Investment Trusts (InvITs)*" issued by SEBI on 5 June 2018 (2018 Guidelines). In supersession of the 2018 Guidelines, the 2019 Guidelines introduce two modes of fund raising by listed InvITs, namely (i) preferential issue and (ii) institutional placement. These are akin to fund raising methods available to companies under the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018 (SEBI ICDR Regulations).

Salient features of the 2019 Guidelines

- I. **Common conditions for a preferential issue / institutional placement:** An InvIT may undertake a preferential issue or an institutional placement upon fulfilment of the following conditions:
 - **Resolution of unitholders:** A resolution of the existing unitholders of the InvIT must be obtained (where votes cast in favour of the resolution shall be not less than one and a half times the votes cast against the resolution, i.e. not less than 60% of the valid votes will need to be in favour of the resolution);
 - **Minimum listing period:** The units of the InvIT must have been listed on a stock exchange: (a) for a period of at least 6 (six) months for a preferential issue; and (b) for a period of at least 12 (twelve) months for an institutional placement, prior to the date of issuance of notice to the unitholders for convening the meeting of the unitholders;
 - **Compliance with continuous obligations:** The InvIT must be in compliance with all the conditions for continuous listing; and the disclosure obligations under the Securities and Exchange Board of India (Infrastructure Investment Trust) Regulations, 2014 (SEBI InvIT Regulations) and circulars issued thereunder;
 - **Maximum number of investors:** Any offer or allotment through a private placement shall not be made to more than 200 (two hundred) investors (excluding institutional

investors as defined under the SEBI InvIT Regulations (Institutional Investors)) in a financial year; and

- **Other conditions:** The promoter(s) or partner(s) or director(s) of the sponsor(s) or investment manager or trustee of the InvIT must not be declared as fugitive economic offenders.

II. Pricing, eligible investors, lock-in, disclosures and other conditions:

- **Pricing and eligible investors:** For the purposes for pricing, the units are categorised into two categories: (i) frequently traded units; and (ii) infrequently traded units. In both cases, 'frequently traded units' are defined as units in which the traded turnover on the relevant stock exchange⁽¹⁾ during the 12 (twelve) calendar months preceding the Relevant Date, is at least 10% of the total number of issued and outstanding units of such class of units of the InvIT. The pricing methodology and eligible investors are further described below:

Preferential Issue	Institutional Placement
Relevant Date	
The date 30 (thirty) days prior to the date on which the meeting of the unitholders is held to approve the preferential issue.	The date of the meeting in which the board of directors of the investment manager decides to open the issue.
Pricing for frequently traded units	
<p>The price shall be not lesser than the higher of: (a) the average of the weekly high and low of the volume weighted average prices of the units quoted on the relevant stock exchange⁽¹⁾ during the 26 (twenty-six) weeks preceding the relevant date; or (b) the average of the weekly high and low of the volume weighted average prices of the units quoted on the relevant stock exchange⁽¹⁾ during the 2 (two) weeks preceding the relevant date.</p> <p>In case of an issuance to less than 5 (five) institutional investors, the price shall not be less than the average of the weekly high and low of the volume weighted average prices of the units on a recognised stock exchange during the 2 (two) weeks preceding the Relevant Date.</p>	<p>The price shall not be lesser than the average of the weekly high and low of the closing prices of the units of the same class quoted on the stock exchange⁽²⁾ during the 2 (two) weeks preceding the relevant date. Akin to a qualified institutions placement under the SEBI ICDR Regulations, a discount of up to 5% may be provided on the price so calculated, subject to approval of unitholders.</p>
Pricing for infrequently traded units	
<p>The price is to be determined taking into account the net asset value (NAV) of the InvIT based on a full valuation of all existing InvIT assets.</p>	

Eligible investors	
Any investor eligible to invest in listed InvITs. A preferential issue shall not be made to any person who has sold or transferred units of the InvIT during the 6 (six) months preceding the Relevant Date.	Only Institutional Investors which per the SEBI InvIT Regulations include qualified institutional buyers; and family trusts and SEBI registered intermediaries having net worth of more than INR 500 crore (Indian Rupees Five hundred crore).
Sponsors, investment managers and persons related to them or their associates are permitted to invest.	Sponsors, investment managers and persons related to them or their associates are not permitted to invest.

⁽¹⁾ 'Relevant stock exchange' as been defined to mean the recognised stock exchange in which the highest trading volume in respect of the units has been recorded in the 26 (twenty-six) week period preceding the relevant date.

⁽²⁾ While for determining whether the units are 'frequently traded' the relevant stock exchange as mentioned in note (1) above is required to be considered, we note that the pricing methodology does not refer to the relevant stock exchange. Accordingly, clarity is required in relation to which stock exchange will be considered for determining the average of the closing prices.

- **Lock-in:** Given that sponsors are allowed to participate in preferential issues, the lock-in requirements in case of preferential issues are distinct from those in institutional placements. The lock-in provisions are detailed below:

Preferential Issue	Institutional Placement
Lock-in investors other than sponsors	
To be locked-in for a period of 1 (one) year from the date of trading approval.	There is no lock-in requirement applicable in case of an institutional placement. However, units allotted shall not be sold by the allottee for a period of 1 (one) year from the date of allotment, except on a recognised stock exchange.
Lock-in for sponsors	
Units allotted (i) in terms of Regulation 12(3) of the SEBI InvIT Regulations shall be locked-in for 3 (three) years (ii) in excess of Regulation 12(3) of the SEBI InvIT Regulations shall be locked in for 1 (one) year, from the date of trading approval. For computing such lock-in requirement, units locked-in as per Regulation 12(3) of the SEBI InvIT Regulations shall be taken into account.	NA

Lock-in of existing units held by allottees	
The entire pre-preferential issue unitholding of allottees shall be locked-in from the relevant date up to a period of 6 (six) months from the date of trading approval.	NA

- **Disclosures and appointment of a merchant banker:** The key difference in the disclosure norms for both modes of issuances is that in case of a preferential issue, the disclosures are required to be made as part of the explanatory statement to be annexed to the notice sent to the unitholders proposing the issuance of units. The disclosures prescribed are similar to disclosures prescribed in case of a preferential issue under the SEBI ICDR Regulations, including, inter alia, objects of the issue, NAV, the maximum number of units to be issued.

In case of an institutional placement, the InvIT is required to prepare a detailed placement memorandum, akin to a placement document in case of a qualified institutions placement under the SEBI ICDR Regulations. The 2019 Guidelines allow disclosures to be included by reference to any earlier offer document, annual report, financial statements, valuation report along with the links to such documents which are available on the websites of the InvIT, the stock exchanges or SEBI. The InvIT is required to appoint 1 (one) or more merchant bankers as lead manager(s) to the institutional placement. The merchant banker(s) are required to submit a due diligence certificate and furnish a copy of the placement memorandum along with any other document required by the stock exchange(s). The format of such due diligence certificate has not been specified in the 2019 Guidelines.

- **Consideration and utilisation of proceeds:** Other than where units are proposed to be issued for consideration other than cash, the prospective allottees are required to pay the full consideration for the units, prior to allotment of the units. All amounts received towards subscription of units are to be kept in a separate bank account and till the listing of such units, such amounts may only be utilised towards adjustment against allotment of units and/or refund of money to the applicants.
- **Other conditions:** Allotment in case of preferential issues is required to be completed within 15 (fifteen) days from the date of passing of the unitholders' resolution whereas in case of an institutional placement, it is required to be completed within 365 (three hundred and sixty-five) days of the unitholders' resolution. Further, an InvIT can make an institutional placement only once every 6 (six) months. However, no such restriction has been prescribed for a preferential issue.

Comment:

The 2019 Guidelines are a welcome and much needed move from SEBI as they provide clarity and solutions to challenges posed to listed InvITs by the 2018 Guidelines. The 2019 Guidelines have fully repealed the 2018 Guidelines and prescribe two fund raising methods, namely preferential issue and institutional placement, which are akin to preferential allotment and qualified institutions placements prescribed under the SEBI ICDR Regulations.

There are, however, a few items which require further clarification, such as the explanatory statement in case of a preferential issue is required to disclose the NAV, but the 2019 Guidelines do not provide the date as on which the NAV needs to be disclosed. Further, the definition of 'frequently traded units' considers units in which the traded turnover during the last **12 (twelve) months** preceding the relevant date is at least 10% of the total number of issued and outstanding units. This does not align with the minimum period of listing required for preferential issues (i.e. 6 (six) months) as mentioned above.

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We also note that the 2019 Guidelines do not allow allotment under institutional placement to sponsors or investment managers or certain related entities. Under Regulation 12(3) of the SEBI InvIT Regulations, the sponsors, are required to hold at least 15% of the outstanding units, post listing for a period of 3 (three) years. In case an institutional placement results in dilution of a sponsor's unitholding below the required threshold, the InvIT will simultaneously need to conduct a preferential issue.

Nevertheless, the 2019 Guidelines provide a great deal of clarity and procedural ease for fund raising under both modes prescribed. SEBI's approach on the pricing methodology also appears to have contemplated a situation for privately placed InvITs which witness very sparse trading volumes. The pricing for infrequently traded units requires the valuer to take into account the NAV and does not prescribe a floor price which provides adequate flexibility in our view. Further, in case of institutional placements, SEBI has permitted disclosures to be included by reference to any earlier offer document, annual report, financial statements, valuation report along with the links to such documents which are available on the websites of the InvIT, the stock exchanges or SEBI. This is a refreshing change from the approach followed by SEBI traditionally in case of offer documents and will make the drafting of the placement memorandum time and cost efficient.

In a nutshell, SEBI's intention to align various requirements to those available to companies under the SEBI ICDR Regulations appears to be a very pragmatic approach and will definitely help listed InvITs raise funds with heightened efficiency.

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