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SEBI REGULATIONS AMENDED TO EASE FUNDING FOR STRESSED COMPANIES

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The Securities and Exchange Board of India (SEBI) has granted certain significant relaxations with respect to new capital raises / preferential allotments by stressed public listed companies. These are effective 22 June 2020, through appropriate amendments to the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 (Takeover Regulations) and the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018 (ICDR Regulations).

Key Relaxations

- **Relaxation of floor price**: The issue price for fresh capital is now based on a lookback of two weeks (instead of higher of two weeks and twenty six weeks) volume weighted average pricing preceding the relevant date i.e. typically the date of board approval.

- **MTO Exemption**: If the capital raise results in a change in control / an acquisition greater than 25% stake in favour of the new investor, there is now a blanket exemption from a mandatory tender offer.

- **Stressed Company**: To qualify as a stressed company, issuer must meet at least 2 out of the following 3 conditions:

  - credit rating downgraded to "D".

  - disclosure of all payment defaults to financial creditors, and where such default has occurred, must have continued for at least 90 days.

  - an intercreditor agreement has been signed in accordance with the 7 June 2019 RBI Restructuring Circular.

- **Public Shareholder Vote**: Majority of public shareholders (present and voting standard) have voted in favour of the capital raise.

- **Use of Proceeds**: Proceeds can neither be used to repay affiliates / promoter nor can the preferential allotment be made in favour of promoters.

- **Lock-in of new securities**: 36 months lock-in from date of trading approval.

Key Considerations

The relaxations granted by SEBI are well crafted to encourage fund infusion into stressed listed companies – a few observations worth considering are below:

Preference Pricing: The 26 week average is invariably higher than the price determined in the 2 weeks preceding the relevant date (given the current state of the listed co); so this rule change could significantly reduce the regulatory floor price for new money investors.

MTO Exemption: Given the deteriorating condition of the stressed listed target, no outlay is now required for a secondary purchase by the new money investor – this also awards greater certainty on final fund flow and equity holding in the target.

Shareholder Approval: Since the proposal will be to aid a stressed target, there is high likelihood of such approvals coming through.

Lock-in: The 36 month lock-in appears to be in lieu of the relaxations granted, this is currently 12 months.

Convertible securities: The amendments are ambiguous as to whether the relaxations are only for issuance of new equity shares, or if they are also applicable to issuance of convertible securities (e.g. convertible bonds / preference shares).

Conclusion:

The relaxation granted by SEBI is expected to play a significant role in stabilizing funding requirements of stressed listed companies, and at the same time grant investors and strategic partners an opportunity to invest in stressed companies at muted valuations – all this without the additional obligation of triggering a mandatory tender offer.

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