

ERGO

Analysing developments impacting business

THE RIGHTS ISSUE PROCESS – SUPPLEMENTED AND SIMPLIFIED

7 February 2020

BACKGROUND

Securities and Exchange Board of India (SEBI) has recently notified amendments to the SEBI (Issue of Capital and Disclosure Requirements) Regulations 2018 and the SEBI (Listing Obligations and Disclosure Requirements) Regulations 2015 to make the rights issue process more efficient and effective, and to reduce the overall time taken to undertake a rights issue, from approximately 55 days to approximately 31 days (the Amendment). Our ERGO on the Amendment can be accessed [here](#). Some of the key changes introduced by the Amendment include (a) discontinuing allotment of securities in a physical manner; (b) mandatory use of Application Supported by Blocked Amount (ASBA) facility as a payment mechanism; and (c) introduction of credit and trading of Rights Entitlements (REs).

SEBI has issued a circular dated 22 January 2020 (Circular) to lay down the procedural requirements for implementation of the Amendment. The Circular provides a detailed framework for credit and trading of the REs, including the renunciation process for a rights issue.

APPLICABILITY

The Circular will be applicable to all rights issues (including those undertaken on a fast-track basis) for which letters of offer is filed on or after 14 February 2020.

RIGHT ISSUE PROCESS

Separate ISIN

Separate ISIN code is to be created for the credit of REs prior to announcement of the record date. Such ISIN shall be kept frozen in the depository system till the opening of the issue and will be permanently deactivated post allotment. However, in cases where the record date has been announced prior to 14 February 2020, the issuers are required to ensure that the letter of offer is filed only after obtaining the ISIN for the REs.

Crediting of REs

Shares held in dematerialised form

Issuers are required to credit the REs, through a corporate action, to the respective demat account of all eligible investors as on the record date prior to the opening of the issue (Eligible Investor).

Shares which are frozen or held in unclaimed suspense account/IEPF authority

In cases where the demat account of the Eligible Investor is frozen or the demat account details are not available or the equity shares are held in unclaimed suspense account or in the account of the Investor Education and Protection Fund, the REs are required to be transferred into a suspense escrow demat account and an intimation to this effect is required to be given by the issuer to the respective Eligible Investor as well as to the registrar.

Shares held in physical form

An intimation will be sent to all shareholders holding shares in physical form to provide their demat account details for crediting of REs. Such details can be provided upto two days prior to closure of the issue. Upon receipt of demat account details, REs will be credited to such demat account at least a day prior to the closure of the issue.

Trading and renunciation of REs

REs shall be traded on the secondary platform of the stock exchanges under a T+2 rolling settlement mechanism. The trading will commence on the date of opening of the issue and shall continue until four days prior to closure of issue. The Eligible Investors can renounce their respective REs (to the extent of REs available in their demat accounts) either by sale of such REs on the stock exchange platform or through an off-market transfer, which will be settled through the depository mechanism.

Application Form

The Circular replaces the erstwhile concept of 'composite application forms' and 'split application forms'. The Eligible Investors and the renounees, will use a common application form for making an application in the issue. The application form will be despatched to all eligible shareholders by the registrar and shall also be available on the website of the registrar. The option of making plain paper applications has been retained for procedural convenience.

One application for each demat account

The Eligible Investors and the renounees are required to submit their respective application forms only using the ASBA mechanism and a single application form is required to be submitted for all REs available in the demat account of the applicant.

Allotment process

SEBI has further introduced the facility for Eligible Investors to correct the bid data collated by self-certified syndicate banks for one day, i.e. on the next working day post issue closure, which is similar to the facility available in initial public offers. This may facilitate a reduction in the number of technical rejections in rights issues going forward. Additionally, the Circular has made the registrar responsible for finalisation of the allocation in the Issue, crediting of shares in the demat accounts of the allottees and issuing refund instructions, as necessary.

Comments

The Circular was much awaited by issuers and market intermediaries involved in on-going and prospective rights issues and comes as a welcome move albeit with certain

operational challenges. It provides much needed clarity on a host of changes introduced by the Amendment.

However, some aspects of the revised process continue to remain ambiguous. Firstly, the Circular does not provide any clarity on the operational control of the suspense demat escrow account. It is unclear whether, upon receipt of demat details, the registrar shall be solely responsible for transferring the REs to the demat account of the investors from the suspense demat escrow account, or will the issuer be required to issue instructions for the same. Secondly, the Circular does not specify whether the details of demat accounts to be provided by Eligible Investors (holding physical shares) is to be provided to the issuer or to the registrar. Lastly, it is unclear whether the securities arising out of existing equity shares which are either under dispute, or currently in abeyance pursuant to a court order or an order of a governmental authority, can be kept in abeyance or do they terminate with the extinguishing of the corresponding REs.

No Eligible Investor holding shares in physical form shall be able to apply in the issue, unless they provide their demat account details at least two days prior to the closure of the issue. This is further to SEBI's efforts to extinguish physical applications and phase away manual intervention in capital market transactions.

Interestingly, both the Amendment and the Circular have not prescribed any reduction of post issue timelines for rights issues.

- *Sudhir Bassi (Executive Director), Aayush Mohata (Principal Associate) and Raghav Bhatia (Associate)*

For any queries please contact: editors@khaitanco.com

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Mumbai

One Indiabulls Centre, 13th Floor
Tower 1 841, Senapati Bapat Marg
Mumbai 400 013, India

T: +91 22 6636 5000
E: mumbai@khaitanco.com

New Delhi

Ashoka Estate, 12th Floor
24 Barakhamba Road
New Delhi 110 001, India

T: +91 11 4151 5454
E: delhi@khaitanco.com

Bengaluru

Simal, 2nd Floor
7/1, Ulsoor Road
Bengaluru 560 042, India

T: +91 80 4339 7000
E: bengaluru@khaitanco.com

Kolkata

Emerald House
1 B Old Post Office Street
Kolkata 700 001, India

T: +91 33 2248 7000
E: kolkata@khaitanco.com