21 February 2024

Indian Companies can now raise capital from all Foreign Investors through Direct Listing in the International Financial Services Centre

INTRODUCTION

The International Financial Services Centre (IFSC) at the Gujarat International Finance Tec-City City is India's first international financial centre. The objective of the IFSC, which has been created through the Special Economic Zones Act, 2005, is amongst others, to onshore the offshore, i.e. to undertake those India related financial activities in IFSC, which are currently carried out outside of India. IFSC aims to be an alternative to other international financial service centres such as London, New York and Singapore, to attract foreign financial services and foreign capital through ease of doing business and tax incentives. The International Financial Services Centres Authority (IFSCA), established by way of the International Financial Services Centres Authority Act, 2019, is the regulator of financial products/services, service providers and other related matters in the IFSC.

Direct Listing Regime for Indian Companies

Unlisted public limited companies incorporated under the Companies Act, 2013 (Cos Act), can now directly list their equity shares on the India International Exchange (India INX) and the NSE International Exchange (NSEIX, and together with the India INX, IFSC Stock Exchanges), in the IFSC. As on date, companies listed in India, cannot list their shares on the IFSC Stock Exchanges, since the Securities and Exchange Board of India (SEBI) is yet to issue the operational guidelines for listed Indian companies, which we understand is under process, and post which even listed companies in India can issue and list their shares on the IFSC Stock Exchanges.

Cos Act Amendments

The amendment of the Cos Act dated 28 September 2020 paved way for companies incorporated in India to list their shares on stock exchanges in foreign jurisdictions. The amendment was brought into force on 30 October 2023 by way of a notification by the Ministry of Corporate Affairs (MCA). Subsequently, the Companies (Listing of equity shares in permissible jurisdictions) Rules, 2024 (Direct Listing Rules) has also been notified on 24 January 2024 by the MCA, which deals with listing of Indian companies on stock exchanges of permissible jurisdictions and lays out certain eligibility criteria. 'Permissible jurisdiction' has been currently defined to mean IFSC. The Direct Listing Rules can be accessed *here*.

Foreign Exchange Laws Amendments

The Central Government by its notification dated 24 January 2024, amended the Foreign Exchange Management (Non-debt Instruments) Rules, 2019 (NDI Rules) by way of the Foreign Exchange Management (Non-debt Instruments) Amendment Rules, 2024 (NDI Rules Amendment). In terms of the NDI Rules Amendment, a person, not being a resident of India, is permitted to hold, purchase and/ or sell shares of a company listed on the IFSC Stock Exchanges. Any category of foreign investor can deal in shares of an Indian listed Company on the IFSC Stock Exchanges. Whereas foreign investors can invest in Indian companies listed on the stock exchanges of India only through the foreign portfolio investor route. Indian residents are not allowed to purchase or sell shares of an Indian company listed on the IFSC Stock Exchanges. Further, the restrictions applicable to foreign investors under Press Note 3 dated 17 April 2020 issued by the Ministry of Commerce and Industry, will also apply to foreign investment in Indian companies listed on the IFSC Stock Exchanges. Accordingly, any investor/ beneficial owner which is a citizen of/ is incorporated in a country sharing a land border with India, can hold shares of an Indian company which is listed on the IFSC Stock Exchanges, only with the approval of the Government of India. The NDI Rules Amendment can be accessed *here*.

The IFSCA Listing Regulations

The IFSCA notified the International Financial Services Centres Authority (Issuance and Listing of Securities) Regulations, 2021 (IFSCA Listing Regulations) on 16 July 2021, which regulates, amongst others, initial public offering of equity shares and convertible securities by an unlisted company incorporated in India, the IFSC or a Foreign

Jurisdiction[1]. The IFSCA Listing Regulations specify the eligibility criteria, mode of undertaking an initial public offering, due-diligence requirements, disclosures in offer documents, minimum offer size, pricing, offer period, minimum subscription, amongst others. IFSCA has sought public comments on the IFSCA Listing Regulations, and we expect changes to these regulations in the near future. The IFSCA Listing Regulations can be accessed *here*.

Certain Key Aspects of Direct Listing of unlisted Indian Companies

Presently, Indian unlisted public limited companies can list on the IFSC Stock Exchanges by way of an initial public offering comprising of a fresh issue and/ or an offer for sale by existing shareholders. The Direct Listing Rules specify certain eligibility criteria, which include *inter alia* that the Indian company: (a) should not be a company incorporated under Section 8 of the Cos Act or a Nidhi under Section 406 of the Cos Act, respectively; (b) should not be a company with a negative net worth; (d) should not have accepted any outstanding deposits from the public as per Chapter V of the Cos Act; (e) should not have defaulted in payment of dues to any bank, public financial institution, debenture holder or other secured creditor; (f) should not have defaulted in filing of an annual return or financial statements under Sections 92 and 137 of the Cos Act, respectively; and (g) should not have any outstanding partly paid-up shares.

The NDI Rules Amendment also prescribe certain eligibility criteria for Indian public companies to issue their equity shares and/or for existing shareholders of Indian public companies to offer their equity shares for sale (Selling Shareholders) on the IFSC Stock Exchanges, which include *inter alia* (i) the company, its promoters, promoter group, directors and Selling Shareholders not being debarred from accessing capital markets and not being a promoter or director of any other Indian company which is debarred from accessing capital markets; (ii) the company, its promoters and directors not being wilful defaulters; (iii) the company not being under inspection or investigation under the applicable provisions of the Cos Act; and (iv) the promoters and directors of the company not being fugitive economic offenders.

In terms of the NDI Rules Amendment, the price of equity shares in an initial public offer by an unlisted Indian company is required to be determined by a book-building process and shall not be lesser than the 'fair market value' as prescribed under the NDI Rules. The IFSCA Listing Regulations also provide for determination of price by way of a book-building process. Once listed on the IFSC Stock Exchanges, further issuance of shares would be based on applicable pricing norms specified in the IFSCA Listing Regulations.

Issue and offer of equity shares of an Indian company on the IFSC Stock Exchanges is subject to the restrictions on prohibited activities and sectoral caps as specified in the NDI Rules. Further, in terms of the NDI Rules Amendment, a foreign investor can hold equity shares of an Indian Company listed on the IFSC Stock Exchanges subject to the limits specified for foreign portfolio investment under the NDI Rules.

In terms of the IFSCA Listing Regulations, companies seeking to list their shares on the IFSC Stock Exchanges through an initial public offer, are required to meet the following prescribed financial eligibility criteria: (i) operational revenue of at least USD 20 million in the preceding financial year and (ii) average pre-tax profit, based on consolidated audited financials, of at least USD 1 million during the preceding 3 financial

[1] As per Regulation 2(h) of the IFSCA Listing Regulations, "Foreign Jurisdiction" means a country, other than India, whose securities market regulator is a signatory to International Organization of Securities Commission's Multilateral Memorandum of Understanding IOSCO's MMOU) (Appendix A signatories) a signatory to bilateral Memorandum of Understanding with the IFSCA, and which is not identified in the public statement of Financial Action Task Force as:

i. a jurisdiction having a strategic Anti-Money Laundering or Combating the Financing of Terrorism deficiencies to which counter measures apply; or
ii. a jurisdiction that has not made sufficient progress in addressing the deficiencies or has not committed to an action plan developed with the Financial Action Task Force to address the deficiencies.

years. Failure to meet such financial criteria will render such companies' ineligible to undertake an initial public offer on the IFSC Stock Exchanges, unlike an initial public offering under the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018 (SEBI ICDR Regulations) which permits companies that do not meet the financial eligibility criteria specified therein to undertake an initial public offer, subject to compliance with stipulated investor allocation methodology. However, start-up companies and small and medium enterprises are eligible to list their shares on the IFSC Stock Exchanges subject to their annual turnover being lower than USD 20 million and USD 50 million respectively, in accordance with the IFSCA listing Regulations, and such companies are not required to meet stipulated operational revenue, average pre-tax profit or similar financial matrix.

The IFSCA Listing Regulations also require companies listed on the IFSC Stock Exchanges to comply with certain continuous listing obligations and disclosure requirements including (a) periodic (i) disclosures of the shareholding pattern; (ii) disclosure of audited standalone and consolidated financial statements for a financial year; and (iii) disclosure of financial statements for the first three quarters of a financial year; (b) certain event based disclosures such as (i) amendments to constitutional documents; (ii) board meetings pertaining to, *inter alia*, dividends, buy-back of securities, fund raising or change in capital (prior intimation); (iii) proceedings of annual and extraordinary general meetings; (iii) resignations of the directors, key managerial personnel or the compliance officer of the Company; and (iv) adverse opinion, disclaimer of opinion or qualified opinion by the auditors on the financial statements, and (c) material events/ information in terms of the policy for determination of materiality of disclosures, adopted by the board of the listed companies in accordance with the IFSCA Listing Regulations.

Dual Listing on Indian stock exchanges and IFSC

The Direct Listing Rules and the NDI Rules Amendment also apply to the Indian listed companies proposing to list on the IFSC Stock Exchanges. The Direct Listing Rules prescribe similar eligibility conditions, as discussed above, for listed Indian companies. The NDI Rules Amendment require Indian listed companies to comply with the regulations to be notified by SEBI. In terms of the NDI Rules Amendment, the pricing of equity shares issued by a company listed on the IFSC Stock Exchanges as well as on the Indian stock exchanges, shall not be lesser than the price at which such equity shares are issued to domestic investors in a corresponding mode of issuance under applicable laws.

Whilst SEBI is in the process of issuing operational guidelines for listed Indian companies to list their shares on the IFSC Stock Exchanges, the IFSCA Report prescribes the following key recommendations:

- Minimum public shareholding: listed Indian companies which seek to list their shares on the IFSC Stock Exchanges should comply with minimum public shareholding norms separately on the Indian stock exchanges and the IFSC Stock Exchanges.

- Promoter contribution: the minimum share capital required to be locked-in by the promoters should be calculated on a combined basis. However, the actual shares locked-in should be listed on the Indian stock exchanges.

- Preferential issue: companies which are listed on the Indian stock exchanges as well as on the IFSC Stock Exchanges, seeking to issue further shares on a preferential basis, should comply with the corresponding provisions of the SEBI ICDR Regulations, to the extent applicable.

- Rights issue: companies which are listed on Indian stock exchanges as well as the IFSC Stock Exchanges, seeking to undertake a right issue should (i) comply with the corresponding provisions of the SEBI ICDR Regulations, to the extent applicable; (ii) be permitted to trade rights entitlements on the IFSC Stock Exchanges in accordance with norms specified by IFSCA; and (iii) price the right shares the same for shareholders on the Indian stock exchanges as well as on the IFSC Stock Exchanges, and to achieve the same, the exchange rate as on the record date should be taken as the reference rate for converting the Indian rupee denominated right issue price into foreign currency.

The IFSCA Report can be accessed *here*.

CONCLUDING REMARKS

The Direct Listing Rules and the NDI Rules Amendment are decisive steps towards establishing a direct and dual listing regime in India through the IFSC. This provides an alternate platform to showcase Indian companies in the global investor community and provides an opportunity to access global funds and investor base, comparatively easily. Unlike initial public offers on the Indian stock exchanges, even high net-worth non-residents can now access Indian securities markets, which will in turn benefit Indian companies. This also provides an opportunity to Indian companies to opt for only foreign public shareholders by listing exclusively on the IFSC Stock Exchanges.

The IFSCA Listing Regulations specify only the broad categories of disclosures in an offer document, and detailed pointwise/ sub-heads of disclosure requirements have not been specified. This provides flexibility to issuer companies, including in relation to the proposed utilisation of the proceeds from capital issues and the consequent disclosures requirements.

In terms of the notification dated 5 March 2020, issued by the Ministry of Finance, capital gains arising out of transfer of equity shares of Indian companies in IFSC is exempted from tax. This is with the presumption that the shares listed shall be denominated in a foreign currency. This could be a tremendous boost for foreign investors to invest in companies listed on the IFSC Stock Exchanges. However, this could also see a shift of foreign investor base from the Indian stock exchanges to the IFSC Stock Exchanges.

Whilst SEBI is yet to prescribe the regulatory framework for listed Indian companies to list on the IFSC Stock Exchanges and other foreign stock exchanges, it is clear that Indian companies exclusively listed on the IFSC Stock Exchanges shall not be subject to other SEBI regulations such as takeover regulations and insider trading regulations. IFSCA may in the future notify the relevant regulations to address these aspects.

The IFSCA Listing Regulations also provide for listing of a company incorporated in a Foreign Jurisdiction, subject to its local laws permitting listing on foreign stock exchanges such as the IFSC Stock Exchanges. Although the IFSC Stock Exchanges are yet to notify the operational guidelines/ rules pertaining to listing of foreign companies, the legal enabler has been created.

- *Aditya Cheriyan, Partner; Oishik Bagchi, Partner and Johann Valladares, Associate*

For any queries please contact: editors@khaitanco.com

AMBITION STATEMENT

"Our ambition is to be a respectable law firm providing efficient and courteous service, to act with fairness, integrity and diligence, to be socially responsible and to enjoy life. We should put greater emphasis on working in consonance with our aforesaid values than on maximizing earnings. Earn we should but with dignity and pleasure."

Khaitan & Co is a premier full-service Indian law firm with 25+ practice areas, over 1,000 lawyers, including 200+ partners. To know more about us, please visit www.khaitanco.com