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Analysing developments impacting business

BOLSTERING THE FRAMEWORK OF SOCIAL STOCK EXCHANGES IN INDIA

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The inaugural listing of a non-profit organisation (NPO) on the social stock exchange (SSE) has set the ball rolling for social enterprises (SE) to raise funds on the SSE. Over 30 NPOs have been registered on the SSE. The experience and learning will help to liberalise the framework and provide impetus to SEs and investors alike to foster impact investing.

Pursuant to recommendations from the Social Stock Exchange Advisory Committee constituted by SEBI and public comments, SEBI vide a circular dated 28 December 2023 (Circular) has modified the extant framework and provided flexibility on aspects related to eligibility criteria, minimum issue, and application size of zero coupon zero principal instruments (ZCZPs) and initial disclosure requirements that are to be met by NPOs issuing ZCZPs. It has also laid down the procedure to be followed by NPOs for public issuance of ZCZPs including prescribing the content to be included in the fund-raising document.

Analysis:

The Circular has eased the norms for listing on SSEs by liberalising the eligibility requirements for NPOs for registration on the SSE, initial disclosure requirements and conditions relating to issuance of ZCZPs, which are discussed below:

A. Minimum requirements for registration on SSE

SEBI has expanded the eligibility criteria for NPOs seeking registration with SSE by allowing entities registered under Section 10(23C) and Section 10(46) of the Income Tax Act, 1961 (Income Tax Act) to be eligible for registration as NPO with SSE. Earlier, only entities registered under Section 12A / 12AA / 12AB of the Income Tax Act and possessing a valid Section 80G registration certificate were eligible for registration as an NPO with the SSE. It was observed that several NPOs such as government funded educational institutions and hospitals are wholly engaged in not-for-profit activities for the benefit of the public but do not possess a Section 80G registration. Such NPOs, merely on account of not possessing a Section 80G certificate would be deprived of the opportunity to raise funds on SSE. Entities which do not possess a Section 80G certificate have now been permitted to register on SSE if they are registered under either Section 10(23C) or 10(46) of the Income Tax Act.

Further, earlier, NPOs with pending notice or ongoing scrutiny by the Income Tax department were ineligible for registration with SSE. The Circular has now rationalised this requirement by permitting NPOs with ongoing scrutiny or pending notices to be eligible for registration subject to disclosure of details of such scrutiny by the entity at the time of application for registration. Such applicants are also required to disclose the status of fines imposed during such scrutiny. SSEs have been empowered to refuse the registration of NPOs if the notices / scrutiny are grave enough to endanger the registration of an NPO under the Income Tax Act or other relevant laws.

B. Initial disclosure requirements

NPOs now have the flexibility to disclose their past social impact in the fund-raising document as per their existing practice. Earlier, an elaborate format to be followed for such disclosure was mandated. However, it was observed that requiring NPOs to report such impact assessment in the specific format would involve unnecessary costs and delay in the listing of NPOs on SSE. Hence, the reporting of past social impact in the fund-raising document is no longer required to be made in SEBI's prescribed format, as long as certain key parameters, which may be determined by the exchanges from time to time, are disclosed.

C. Procedure and conditions for issue of ZCZPs

The Circular has amended the threshold of minimum issue and application size of ZCZPs along with restricting the transferability of ZCZPs.

➤ **Minimum Issue Size:** The minimum issue size for ZCZPs has been reduced from INR 1,00,000,00 to INR 50,00,000.

➤ **Minimum Application Size:** The minimum application size for subscribing to ZCZPs has been reduced from INR 2,00,000 to INR 10,000.

It is expected that the reduction in the minimum issue and application size will enable more participation from smaller NPOs and retail investors to access SSEs platform for raising capital.

➤ **Minimum Subscription:** There has been no change in the position on minimum subscription to be achieved. The current requirement is that if the NPO does not achieve a subscription of more than 75% of the issue size, the subscription amount received shall be refunded to the investor. It appears that the requirement of refund could be harsh for the NPO considering the time and costs involved in the fund-raising process. Further one of the objectives of the SSE is to facilitate the NPO in raising capital ([which is normally difficult for NPOs to raise](#)). The requirement of refund could be reconsidered by allowing the NPO to extend the time to achieve the minimum subscription. This will allow the NPO to reap maximum benefit of the fund-raising opportunity. The regulator could also consider mandating that until the minimum subscription level is achieved, the funds received shall be held in an escrow account.

➤ **ZCZP Issuance Activity:** The activity for issuance of ZCZP by an NPO through an offer on the SSE has been set out in the Circular.

- the NPO is required to file the draft fund-raising document with the relevant SSE where it is registered;
- pay applicable fees and seek in-principle approval for listing its ZCZP on the SSE;
- the draft fund-raising document will be made available on the website of both the SSE and the NPO, for a minimum period of 21 days for public comments;
- the relevant SSE will provide its observations within 30 days from the date of filing or the receipt of clarifications, whichever is later;
- the NPO will incorporate SSE's observations in the final fund-raising document which is to be filed with SSE before opening of the issue; and
- The final fund-raising document will contain all material disclosures and any other additional disclosures that may be prescribed such that investors can make an informed choice on whether to invest in such NPO.

D. Restriction on transferability of ZCZPs

ZCZPs cannot be transferred from the original subscriber of the ZCZP till the expiry of the tenure of the instrument.

Conclusion

The Circular endeavours to make philanthropy on the bourses more accessible to investors. Liberalising the framework of SSE will not only assist SEs but also contribute towards raising capital for sustainable impact development goals. The Circular succeeds in relaxing certain requirements, and it continues to mandate governance and disclosure norms in the interest of investor protection. It will be interesting to see if the liberalisation in the framework will enable the platform to gain momentum.

- *Nikhilesh Panchal (Partner), Gaurang Mansinghka (Associate) and Prerna Hegde (Associate)*

For any queries please contact: editors@khaitanco.com