Why Price Protection Will Be A Shot In The Arm For Dealmaking In India

By Abhishek Dadoo Gaurang Mansinghka Krithika Kataria

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(From left) Khaitan & Co's Abhishek Dadoo, Gaurang Mansinghka and Krithika Kataria volatility in the market price of the listed target. This, in turn, tends to significantly impact the deal commercials, as an uptick in the market price results in an increase in overall deal value (for instance, increased floor price for a preferential issue or total financial commitment for an open offer).

At the same time, a delta between the commercially agreed price and market price of the listed target would typically result in tax leakage, resulting in a further increase in deal cost.

Certain recent amendments across various regulations of the Securities and Exchange Board of India (SEBI) have elegantly plugged this folly by mandating rumour verification and, at the same time, offering price protection. This ensures information symmetry between the deal team and public shareholders (achieved through rumour verification) and ring-fencing deal commercials (by artificially readjusting any price increase triggered by the rumour verification).

This new regime is already in effect for the top 100 listed entities from 1 June 2024 and will become applicable to the next 150 listed entities from 1 December 2024.

Analysis

The SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (LODR regulations) have been amended to address the rumour verification requirement (RVR). In brief, it states that certain top listed entities are now obligated to continuously monitor specific the news or information with the stock exchanges within 24 hours of the material price movement.

To counteract the potential impact on the market price of the listed target caused by the RVR, SEBI has set out a price protection framework in a circular dated 21 May 2024. Meanwhile, industry associations ASSOCHAM, CII and FICCI have collectively released an ‘Industry Standards Note’ on verification of market rumours. This industry note sets out the standard operating procedure for compliance with the RVR and price protection.

Availability of price protection

Price protection can be availed by a listed entity only when it confirms a rumour within 24 hours from the trigger of material price movement. It is available for events such as preferential issue, qualified institutions placement, open offer, delisting, buyback, scheme of arrangement involving a listed entity and any other transaction where the pricing is regulatorily required to be linked to the traded price of the scrip.

Further, in addition to the shares of the listed entity verifying the rumour, the benefit of price protection will also be available in respect of shares

Identifying the unaffected price

The SEBI circular outlines the process for computing the adjusted volume-weighted average price (VWAP) to determine the unaffected price, by eliminating price fluctuations caused by market rumours. In essence, the adjusted price is an artificial price which excludes the material price movement due to the rumour in the market.

For the purposes of price adjustment, the variation in WAP from the day of the material price movement until the next trading day after rumour confirmation is excluded. The WAP for this variation period is the same as the daily WAP of the trading day preceding the day of material price movement. The price adjustment formula is also linked to the relevant date of a specified transaction and circuit filters of the stock.

Stages and timeline for price protection

The industry note provides that the benefit of price protection can be availed only when an M&A transaction is at an advanced stage. As per the note: (i) multi-party bid process; (ii) selection of the final bidder and agreement on material deal terms; (iii) signing of a binding term sheet; and (iv) all material commercial terms having been agreed and the management having decided to take the transaction for final board approval, are considered as advanced stages of an M&A deal.

The note also provides that price protection will be available for: (i) 180 days, in case of a multi-party bid process, from the rumour verification date if it has been confirmed by the listed entity or any of the bidders; or (ii) 60 days, in any of the advanced stages other than a multi-party bid process, from the rumour verification date.

Conclusion

Price volatility not only makes the retail investors vulnerable but also impacts the commercial viability of undertaking a transaction. The introduction of a rumour verification and price protection regime is a strategic measure to promote fair price discovery by mitigating the disruptions caused by price swings. The amendments provide much needed clarity enabling public investors to make informed decisions by curbing information asymmetry.

While additional regulatory clarifications may be required on aspects such as method of calculating material price movement, specificity of rumour, identifying intricate rumours and their impact on the price etc., the regulatory regime on rumour verification and price protection is set to play a pivotal role in shaping the public M&A deal market in India.

Abhishek Dadoo is Partner, and Gaurang Mansinghka and Krithika Kataria are associates at law firm Khaitan & Co. Views are personal.

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