

Consultation Paper on

Review of the Regulatory Framework for Debenture Trustees (DTs)

1. Objective

The objective of the consultation paper is to seek comments/ views from the public on the proposals that are intended to strengthen the regulatory framework for Debenture Trustees (DTs) as well as empower the DTs to effectively discharge their responsibilities towards the debenture holders of listed debt issues / proposed to be listed debt issues.

2. Background

SEBI intends to review the regulatory framework for DTs and put in place provisions that would further secure the interests of the debenture holders of listed debt issues, enable the DTs to perform their duties in the interest of the investors more effectively and promptly and also aid in taking a step forward towards creating and sustaining a vibrant market for debt securities. SEBI has also held discussions with representatives of various DTs, other market participants/ stakeholders to understand their concerns and suggestions. It has been observed that there have been cases of delay in enforcing the security in the event of default, which is detrimental to the interests of the investors. Data received from the Trustee Association of India (TAI) indicates that the DTs have been able to enforce the security successfully in around 35% of the issues that have defaulted in the past 5 financial years, thereby building the case for strengthening the framework for DTs and ensuring co – operation from the Issuers to enable the DTs to act swiftly in taking corrective measures in the interests of the investors.

The Consultation Paper takes into account suggestions from the various stakeholders and lists down proposals for public comments, along with detailed rationale for the same

3. Proposals

3.1. Enhancement of net-worth requirement for DTs:

Minimum net worth requirement to be eligible for grant of registration as a DT to be increased to ₹ 10 Crores, from current requirement of ₹ 2 crores. The existing registered

DTs having a net worth of less than rupees ₹ 10 crores, shall be provided a period of three years to meet the said net worth requirement.

Rationale:

Currently, as per DT Regulations, an applicant, desirous of getting registered as DT, is required to have a minimum net-worth of ₹ 2 Crores to be eligible for grant of registration as a DT, and the same has to be maintained at all times during the period of registration. DTs have an onerous responsibility of working in the interests of the investors through careful monitoring of the covenants of the trust deed and ensuring that regular interest/principal payments are made to the debenture holders along with complying with various Regulations, Circulars, etc. On account of these enormous administrative, legal and enforcement related duties are cast on the DTs. In order to ensure efficient and effective discharge of the same, it is necessary that financially sound entities are granted registration as DTs.

With the development of the corporate bond market in India, the responsibilities and obligations of DTs have increased manifold over the years, and their relevance in the system is only expected to increase further.

Accordingly, it is proposed that the minimum net worth requirement to be eligible for grant of registration as a DT may be increased to ₹ 10 Crores.

3.2. Additional interest to debenture holders for non – creation of charge on security within the prescribed timelines

In case an Issuer is unable to create the charge on security in favour of DT within the timelines as specified in the SEBI Regulations/ Companies Act/ Trust Deed, the issuer shall pay additional interest to the debenture holders, for the period till such charge is created. The additional interest shall be specified in the Trust Deed and disclosed in the Offer Document.

Rationale:

Creation of charge on security is of foremost importance in a secured debenture. The debenture holders subscribe to such issue under the comfort that the issuer has kept aside

security to fulfill its payment obligations even in the event of issuer defaulting on its interest/redemption payment obligations.

As per Companies (Share capital and debentures) Rules 2014 and SEBI (Issue and Listing of Debt Securities) Regulations, 2008, a debenture trust deed for securing the issue of debt securities in favour of the DT has to be executed by the issuer within three months of the closure of the issue.

It has been observed that in the past that there have been cases where there have been delays in creation of charge on the security in favour of DT within the aforementioned specified timelines in spite of regular follow up by the DTs or the issuer has defaulted on creation of charge, resulting in losses to the investors. In such cases, the debenture cannot be treated as a secured debenture and would therefore attract a higher interest rate akin to it being an unsecured debenture. The higher interest rate shall be applicable for the period of non-creation of charge.

3.3. Disclosure of compensation arrangement with clients by DTs on their websites

DTs shall disclose the nature of compensation arrangements with their clients on their websites. The disclosure shall include the minimum fee that a DT will charge and factors determining the fee charged.

Rationale:

With the growth and development of the corporate bond market, the scope of work of DTs has enhanced and today DTs are responsible for providing various services/ facilities like, data maintenance, monitoring of the issue, information sharing with CRA/ SEBI, enforcement actions etc. However, it has been observed that many DTs, in a bid to outdo competition, charge very low fee for the issue, which in turn affects the quality of the work done by DTs. It hampers the ability of the DT to monitor the issue for timely payment and in securing the interests of the debenture holders at the time of default thereby putting the interests of the investors at a huge risk.

In a bid to bring transparency in the market and to make investors aware of the likely price structure being charged and its likely impact on the quality of services being offered by the

DT, it is proposed that DTs shall disclose the nature of compensation agreement with its clients, including the minimum fee to be charged (in absolute terms or as a percentage of the issue size) and factors determining the same.

3.4. NOCs from other lenders for creation of charge on security

For creation of charge on the security in favour of DT, no objection certificate shall be obtained from other charge holders on a security before opening of the issue.

Rationale:

The creation of charge on the security is of paramount importance for securing the interest of debenture holders. It has been observed that at times the creation of charge on the security is delayed on account of not obtaining NOCs from other lenders having charge on the same security. In such a situation, either a sub charge is created in the favour of DT or no charge is created, which is not in the interest of the investor. Therefore, it must be ensured that charge on security is created on priority and in the time limit specified under the relevant SEBI regulations. Obtaining NOCs from other such lenders forthwith prior to the opening of the issue will ensure prompt creation of charge on security and early registration of charge with RoC. It is therefore proposed that in cases where there are other charge holders on the same security, issuers shall obtain no objection certificate (NOC) from other charge holders on that security and provide the same to the DT before opening of the issue.

3.5. No requirement for meeting of debenture holders in case of default in public issues

In case of public issues, there shall be no requirement of calling for a meeting of debenture holders in the event of default by the Issuer and the DT can directly enforce the security without obtaining any consent from the debenture holders.

Rationale:

As per the requirements of SEBI (DT) Regulations, 1993, DTs are obligated to call or cause to be called by the body corporate, a meeting of all the debenture holders pursuant to happening of any event, which constitutes a default. During such meetings, consent of the

holders is taken for enforcing the security. In case of a public issue where retail investors form a significant part of the subscriber base, while it is necessary that the security is expeditiously enforced, it is observed that taking such consent of debenture holders at times delays the process as these large number of investors are geographically widely spread. It is, therefore, proposed to do away with the requirement of calling meeting of debenture holders in the event of default in public issue. The DT would therefore be empowered to directly enforce the security without obtaining any consent from the debenture holders in case of public issues. This shall also bring the requirements in line with Company (Share Capital and Debentures) Rules, 2014, which states, inter – alia, that the requirement of calling such meetings shall not be applicable to the public offer of debentures.

3.6. E- voting for obtaining consent of debenture holders

E – Voting shall be considered a valid option for obtaining the consent of debenture holders wherever applicable.

Rationale:

As a practice, DTs obtain the consent of debenture holders while taking decisions of significance, such as enforcement of security post default by an issuer, for which a meeting of the debenture holders is called by the DT. However, it has been noticed that very few debenture holders turn up for the meeting, which constrains the DT's ability to take any decision and also poses the problem of the decision not representing the view of the majority of the holders. To enable the DTs to tide over the difficulty of ensuring presence of all debenture holders in the meeting, it is proposed that e - voting may be considered by the DTs for obtaining consent of the debenture holders. This will not only enable a wider participation of the debenture holders but also lead to early and smooth decision on the course of action to be taken by the DTs.

3.7. Calendar of interest/ redemptions, due and paid, to be displayed on the website of DT(s) for the financial year.

DT shall display on their website the details of interest/ redemption due to the debenture holders in respect of all issues during a financial year within 5 working days of start of financial year. The DT shall also include the details of interest/ redemption due of new issues brought out during the financial year within 5 days of closing of the Issue. Status of payment shall be updated in the calendar by the DT not later than 1 day from the due date of payment. In case the payment is made with a delay by the issuer, the DT shall update the calendar specifying the date of such payment, with a remark 'delayed payment'.

Rationale:

Currently, there is no defined platform where the status of payments made by the Issuers can be readily accessed. Availability of such a platform shall assist the stakeholders and the market participants like Credit rating agencies, Research analysts in keeping track of the financial health and payment of the Issuer. This shall ensure prompt dissemination of information regarding delays in payments/ redemptions by the Issuers and shall also enable debenture holders in following up with the DT as well as in making additional efforts for regularizing the payments. Such disclosures shall also ensure transparency in the conduct of the DTs and the issuers.

3.8. Extension of time for Issuer for submitting certificate signed by DT in accordance with Regulation 52 (5) of SEBI (LODR) Regulations, 2015

After intimation to stock exchanges, the issuer shall furnish its financial results to its DT on the same day. The issuer shall have a period of seven working days from the date of submission of financial results to the stock exchange(s), to file the certificate from the debenture trustee that it has taken note of the contents, as proposed in regulation 52(5) of LODR.

Rationale:

As per Regulation 30 (6) of SEBI LODR Regulations, the company that has listed its shares, is required to submit the outcome of the Board Meeting along with financial results to Stock Exchanges within 30 minutes of the meeting. As per Regulations 52 (1) and 52 (4) of SEBI LODR Regulations, the company that has listed its debentures, has to submit the financial results along with other details to stock exchanges within 45 days from the from the end of

half year. Further as per Regulation 52 (5) of SEBI LODR Regulations while submitting this information, the company has to submit a certificate signed by the DT that it has taken note of the contents submitted to the Stock exchanges.

The issuers that have listed their shares and debentures insist that the DTs issue the aforementioned certificate within 15 minutes of issuer's Board Meeting to enable them to submit the same to stock exchange within 30 minutes. Considering the fact that the DTs are acting for a number of issues, DTs have expressed their inability to certify the information submitted to the DTs by the issuers within 30 minutes. Therefore, it is proposed that issuers that have their shares also listed shall provide the financial results to DTs on the same day, post intimation of the same to the stock exchange(s). Thereafter, issuers shall have a period of seven working days from the date of submission of financial results to the stock exchange(s), to file the certificate from the debenture trustee that it has taken note of the contents, as required vide regulation 52 (5) of LODR.

3.9. Furnishing of updated list of debenture holders to the DT by Issuers/ Registrars to an Issue and Share Transfer Agent (RTA)

The RTA / Issuers shall forward the list of debenture holders to the DT at the time of allotment and thereafter on a monthly basis on the first working day of every next month.

Rationale:

Generally DTs incorporate a clause in the agreement signed with the Issuer that requires the Issuer to submit details of debenture holders at the time of allotment. Further Companies Act mandates that the issuers shall provide list of debenture holders in their periodical reports to the DTs. However, most of the times this information is either not provided or provided with delay to the DTs. Further, when an Issuer defaults or is close to default, the issuer does not co-operate with the DT to provide latest list of debenture holders. The DT, therefore, does not have updated details of debenture holders, in the absence of which, the DT is unable to communicate any relevant information to those debenture holders whose details are not available with the DT.

In order to provide an alternative source for obtaining and verifying the details provided by the issuer, it is proposed that RTAs shall also submit details of debenture holders to the DT at the time of allotment and on a monthly basis on the first working day of each month thereafter, to assist the DTs in contacting the debenture holders promptly.

4. Public Comments:

Public comments are invited on the proposals contained in the Consultation Paper in the following format:

Name of entity/ person/ intermediary/ organization: _____			
Sr. No.	Pertains to Point No.	Comments/ suggestions	Rationale

Comments/ suggestions may be forwarded by email to comments@sebi.gov.in or sent by post to the following address latest by November 16, 2018:

Deputy General Manager

Division of Supervision 3

Market Intermediaries Regulation and Supervision Department

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