



Consultation Paper

**Pricing of Preferential Issues and exemption from open offer for acquisitions
in Companies having Stressed Assets**

1. Objective

1.1. The objective of this discussion paper is to seek comments / views from all stakeholders including listed companies, market intermediaries and public on pricing of Preferential Issues and exemption from making an open offer for acquisitions in listed Companies having Stressed Assets.

2. Background

2.1. It has been observed that listed companies that are facing financial stress are generally, in need of fund infusion to tide over the stress situation and thereby avoid Insolvency/Bankruptcy. Such listed companies face certain difficulties in raising capital through the conventional means. It is observed that, typically, listed companies having “stressed assets” experience progressive fall in their share price. The disclosures that are made by stressed companies such as their financial results, default in servicing debts may also aggravate the fall. This lack of funding at such a crucial stage may lead to a major disruption in functioning of the operations of the company.

2.2. Such companies are often in urgent need of capital from willing financial investors, as other sources of funds tend to dry out at this stage. One method available for raising capital can be through preferential allotment to help resuscitate the company.

2.3. The pricing guidelines for preferential issues which were first introduced on August 04, 1994 mandated that the issue price shall not be less than average of weekly high and low for 26 weeks and average of weekly high and low for 2 weeks preceding the relevant date. Currently, the pricing of preferential issue is mandated under SEBI (Issue of Capital and Disclosures Requirement) Regulations, 2018. In terms of Regulation 158(2) of the SEBI (ICDR) Regulations, 2018, an exemption from pricing of preferential issue is available in case the same has been made in terms of the resolution plan approved under Insolvency and Bankruptcy Code, 2016.

2.4. The pricing provisions in respect of frequently traded scrips under chapter V of the ICDR Regulations, 2018 state as follows:

164. (1) If the equity shares of the issuer have been listed on a recognised stock exchange for a period of twenty six weeks or more as on the relevant date, the price of



the equity shares to be allotted pursuant to the preferential issue shall be not less than higher of the following:

a. the average of the weekly high and low of the volume weighted average price of the related equity shares quoted on the recognised stock exchange during the twenty six weeks preceding the relevant date; or

b. the average of the weekly high and low of the volume weighted average prices of the related equity shares quoted on a recognised stock exchange during the two weeks preceding the relevant date.

2.5. It has been represented that the pricing guidelines are too onerous for any financial investor to consider investments in a stressed company. The rationale for such representation is that the determination of the pricing covers a period of twenty-six weeks or more for frequently traded shares. This large latency in pricing period especially given the deteriorating financial condition of the listed company leads to a wide gap in pricing between the price at the beginning of the twenty-six weeks and the current price when funds are required to be raised.

2.6. In view of the continuous fall in prices in companies having stressed assets, the pricing determined by Regulation 164(1)(a) is higher than as determined by Regulation 164(1)(b). This is because Regulation 164(1)(a) takes in to account average of the weekly high and low of volume weighted average price for 26 weeks as compared to only 2 weeks for Regulation 164(1)(b).

2.7. Given these pricing regulations, it is practically difficult if not impossible for such companies to raise funds through preferential allotment route.

2.8. While, the preferential issue regulations allow preferential issue of specified securities to Qualified Institutional Buyers (QIBs) at “*not lower than average of weekly high and low of the volume weighted average price during the two weeks preceding the relevant date*”, the same has been restricted to 5 QIBs. It has been represented that in the case of such stressed companies, limiting preferential issue only to 5 QIBs is restrictive and excludes other financial investors who may like to participate in such a company at the above pricing methodology.

2.9. A case is also made by such investors to have a substantial holding in the company, in order to take control over the operations of the company and guide the company out of the stress. However, this acquisition of substantial holding and control triggers the obligations by such investor to make open offer to the other investors in terms of the SEBI (SAST) Regulations which require him to acquire 26% more shareholding.



2.10. The relevant regulations of SEBI (SAST) Regulations, 2011 are as follows:

Substantial acquisition of shares or voting rights.

3(1) No acquirer shall acquire shares or voting rights in a target company which taken together with shares or voting rights, if any, held by him and by persons acting in concert with him in such target company, entitle them to exercise twenty-five per cent or more of the voting rights in such target company unless the acquirer makes a public announcement of an open offer for acquiring shares of such target company in accordance with these regulations.

Offer Size

7. (1) The open offer for acquiring shares to be made by the acquirer and persons acting in concert with him under regulation 3 and regulation 4 shall be for at least twenty six per cent of total shares of the target company, as of tenth working day from the closure of the tendering period:

Provided that the total shares of the target company as of tenth working day from the closure of the tendering period shall take into account all potential increases in the number of outstanding shares during the offer period contemplated as of the date of the public announcement:

Provided further that the offer size shall be proportionately increased in case of an increase in total number of shares, after the public announcement, which is not contemplated on the date of the public announcement.

Offer Price

8(2) In the case of direct acquisition of shares or voting rights in, or control over the target company, and indirect acquisition of shares or voting rights in, or control over the target company where the parameters referred to in sub-regulation (2) of regulation 5 are met, the offer price shall be the highest of,—

(a) the highest negotiated price per share of the target company for any acquisition under the agreement attracting the obligation to make a public announcement of an open offer;

(b) the volume-weighted average price paid or payable for acquisitions, whether by the acquirer or by any person acting in concert with him, during the fifty-two weeks immediately preceding the date of the public announcement;

(c) the highest price paid or payable for any acquisition, whether by the acquirer or by any person acting in concert with him, during the twenty-six weeks immediately preceding the date of the public announcement;



(d) the volume-weighted average market price of such shares for a period of sixty trading days immediately preceding the date of the public announcement as traded on the stock exchange where the maximum volume of trading in the shares of the target company are recorded during such period, provided such shares are frequently traded;

(e) where the shares are not frequently traded, the price determined by the acquirer and the manager to the open offer taking into account valuation parameters including, book value, comparable trading multiples, and such other parameters as are customary for valuation of shares of such companies; and

(f) the per share value computed under sub-regulation (5), if applicable.

2.11. It has been represented that making an open offer will create substantial financial obligation for an incoming investor in addition to infusion the investor has made in the stressed company and will increase the cost of financial intervention to avoid insolvency. A case is therefore made out to relax the conditions of making an open offer.

2.12. Presently, in terms of Regulation 10(1)(da) of the SEBI(SAST) Regulations, open offer obligations are exempted in case of acquisition pursuant to a resolution plan approved under section 31 of the Insolvency and Bankruptcy Code, 2016.

3. **Proposal**

3.1. The matter was deliberated at the Primary Market Advisory Committee (PMAC), which has identified three key issues i) an objective criteria for determining a company as stressed, ii) a reasonable pricing for preferential allotment and iii) exemptions from open offer obligations. The PMAC has recommended that SEBI may seek public comments on its following recommendations for exemption in pricing of preferential issue and from making an open offer in case of allotment to non- promoters:

3.2. A listed entity satisfying any two out of the following three conditions shall be considered as stressed

3.2.1. Any listed company that has made disclosure of defaults on payment of interest/ repayment of principal amount on loans from banks / financial institutions and listed and unlisted debt securities for two consequent quarters in terms of SEBI Circular dated November 21, 2019.



3.2.2. Existence of Inter-creditor agreement in terms of Reserve Bank of India (Prudential Framework for Resolution of Stressed Assets) Directions 2019 dated June 07, 2019.

3.2.3. Downgrading of credit rating of the listed instruments of the company to “D”

3.3.A listed entity complying with conditions mentioned at 3.2 above, shall be eligible for exemptions as follows:

3.3.1. Proposed exemption under ICDR

Exemptions may be provided to eligible listed entities from strict enforcement of pricing related regulations under Chapter V (Preferential Issue) of the ICDR Regulations. However, the pricing in such cases may be determined as follows:

Pricing:

- (i) not less than the average of the weekly high and low of the volume weighted average prices of the related equity shares quoted on a recognised stock exchange during the two weeks preceding the relevant date.

3.3.2. Proposed exemption under SAST

Exemption from making an open offer may be considered for the allottees of preferential issue in such aforesaid stressed companies if the acquisition is beyond the limit prescribed in terms of Regulation 3(1) of SAST Regulations

3.4. Listed companies complying with conditions mentioned at 3.2 above, shall ensure the following in order to avail above mentioned exemptions:

3.4.1. The preference issue is made to persons/entities that are not part of the promoter or promoter group on the date of the board meeting to consider the preferential issue

3.4.2. Resolution for the preferential issue at the aforesaid pricing and exemption from open offer has been approved by the majority of minority shareholders (i.e., excluding the promoters, the promoter group and any proposed allottee in the preferential issue that may already hold specified securities in the listed company prior to the preferential issue)



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3.4.3. Proposed use of proceeds of such preferential issue will be disclosed in the explanatory statement sent for purposes of the shareholder resolution

3.4.4. Monitoring agency will be appointed for monitoring use of the proceeds of such a preferential issue

3.4.5. The shares issued to the investors in such an issue shall be locked in for a period of three years from the latest date of trading approval granted by all the stock exchanges where the specified securities are listed.

4. **Public comments**

4.1. Considering the implications of the said matter on the market participants including issuer companies and investors, public comments are invited on the proposed option at Para 3 above. Comments may be sent by email or through post, in the following format :

Name of entity / person : Contact Number & Email Address :			
Sr. No.	Reference Para of the consultation paper	Suggestion/ Comments	Rationale

While sending email, kindly mention the subject as "**Pricing of Preferential Issues and exemption from open offer for acquisitions in Companies having Stressed Assets**".

The comments may be sent by email to Shri Abhishek Rozatkar (abhishekr@sebi.gov.in) or sent by post at the following address latest by May 13, 2020:

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