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SEBI modifies modus operandi for listed companies proposing to enter into scheme of arrangement under sections 391-394 or 101 of the Companies Act, 1956. The Regulator has drawn new set of guidelines, driven with the motive of better corporate governance and investor protection

In brief

The Securities and Exchange Board of India (SEBI or the Regulator) has issued a Circular¹ on 4 February 2013, replacing the existing guidelines for listing of an unlisted entity pursuant to any scheme of arrangement (the Scheme) entered into by a listed company with an unlisted entity under sections 391-394 or 101 of the Companies Act, 1956.

¹ CIR/CFD/DIL/5/2013 issued on 4 February 2013

Existing guidelines

In order to bring the uniformity in the applications submitted to SEBI for listing, it had issued a Circular dated 3 September 2009². The said Circular clearly laid down the minimum requirements for any company to seek relaxation from the strict enforcement of the conditions mentioned under Rule 19 of Securities Contracts (Regulation) Rules, 1957 (SCRR), which are as under:

² SEBI/CFD/SCRR/01/2009/03/09 dated 3 September 2009

- The unlisted entity (transferee entity) issues the equity shares to the shareholders of listed transferor company in compliance with the scheme approved by the High Court,
- Atleast 25% of the post scheme paid-up share capital of the unlisted transferee entity comprises of shares allotted to the public shareholders in listed transferor company,
- There are no outstanding warrants or instruments which gives rights to any person to take equity shares of the unlisted transferee entity at any future date.

Unlisted transferee entities are required to submit an application for listing to the stock exchange(s). The designated stock exchange was required to forward the said application to the Regulator along with its recommendations/modifications. The Regulator would then grant the relief, along with the conditions as it may deem necessary.

New guidelines (applicable with immediate effect)

The Regulator has expressed concerns after it received certain applications seeking relaxation which could have adversely affected the interest of minority shareholders. SEBI has therefore, modified the modus operandi providing a set of comprehensive requirements for seeking exemption.

Summarised below are the key requirements arising from the new Circular:

- Listed company proposing to undertake any scheme is required to submit the draft scheme to the designated stock exchange along with the following documents:
 - Valuation report from an independent Chartered Accountant;

- Report 3 from the audit committee recommending the scheme taking into consideration the above mentioned valuation report;
- Fairness opinion by a merchant banker;
- Pre and post Scheme shareholding pattern of the transferee unlisted entity;
- Audited financials for last 3 years of the transferee unlisted entity;
- Complaints Report 4 summarising the status of complaints received and their status;
- Compliance with clause 49 of the listing agreement.

- The designated stock exchange shall forward draft Scheme alongwith other documents and their objection/no objection letter to SEBI. Further, it shall issue the observation letter to the company after incorporating the comments received from SEBI. The designated stock exchange and SEBI can also seek an opinion from an independent Chartered Accountant;
- **Company is required to incorporate this observation letter in the notice sent to the shareholders seeking approval of the scheme;**
- Companies would be required to disclose the draft scheme along with the documents submitted to the stock exchange and the observation letter received from the stock exchange, on its website within 24 hours of receiving the same.
- All the schemes submitted by the company should provide for obtaining shareholder approval through postal ballot and e-voting. **The new circular also provides that, atleast two-third of the votes cast by the public shareholders must be in favour of the scheme.**
- Once the scheme is approved by the High Court, the listed company shall submit its application under sub-rule 7 of Rule 19 of the SCRR seeking for the

³ New requirement as compared to the previous guidelines

⁴ New requirement as compared to the previous guidelines

relaxation from strict enforcement of the conditions mentioned under Rule 19 of the SCRR. Such application would be accompanied with the following documents:

- Copy of the approved Scheme;
- Result of voting by the shareholders;
- Statement explaining the changes in the approved Scheme vis-a-vis the draft Scheme;
- Status of compliance with Observation Letter;
- Complaints report in the prescribed format.

- **Applicability of the new Circular** – The new Circular would be applicable with the immediate effect. All the schemes, not yet submitted to the High Court are required to be comply with the new Circular, irrespective of whether the draft scheme has already been approved by the designated stock exchange.
- **Miscellaneous** – The new Circular also reiterates the guidelines with respect to the issue of equity shares with differential voting rights and the warrants along with non-convertible debentures, without making an initial public offer for the respective securities. These guidelines are identical to the guidelines mentioned under the *erstwhile* Circular of 2009. Since the said Circular stands repealed, the said guidelines will take effect through the new Circular.

Key takeaway

For the listed entities having already obtained the no objection from the stock exchange, but are yet to file the scheme with the High Court; the new guidelines mandate them to again comply with the fresh requirements as above. This may consume additional time period.

The new guidelines also prescribe that atleast two-third of the votes cast by the public shareholders must be in favour of the scheme. *Prima facie* this requirement is in addition to the existing requirements under the Companies Act, 1956.

The new guidelines are certainly a welcome one considering the Regulator's objective of having increased corporate governance and the investor protection. However, one may expect more visibility on the precise time frame within which the stock exchange and the Regulator may take in issuing the observation letter. While the guidelines are self explanatory and unambiguous, it needs to be seen if the proposed process can be completed within a reasonable time period in order to protect the interest of all the stakeholders as also the minority shareholders.

Our offices

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<p>Ahmedabad President Plaza, 1st Floor Plot No 36 Opp Muktidham Derasar Thaltej Cross Road, SG Highway Ahmedabad, Gujarat 380054 Phone +91-79 3091 7000</p>	<p>Bangalore 6th Floor, Millenia Tower 'D' 1 & 2, Murphy Road, Ulsoor, Bangalore 560 008 Phone +91-80 4079 7000</p>	<p>Bhubaneswar IDCOL House, Sardar Patel Bhawan Block III, Ground Floor, Unit 2 Bhubaneswar 751009 Phone +91-674 253 2279 / 2296</p>	<p>Chennai 8th Floor, Prestige Palladium Bayan 129-140 Greams Road, Chennai 600 006 Phone +91-44 4228 5000</p>	<p>Hyderabad #8-2-293/82/A/113A Road no. 36, Jubilee Hills, Hyderabad 500 034, Andhra Pradesh Phone +91-40 6624 6600</p>
<p>Kolkata 56 & 57, Block DN. Ground Floor, A- Wing Sector - V, Salt Lake. Kolkata - 700 091, West Bengal, India Telephone: +91-33 2357 9101 / 4400 1111 Fax: (91) 033 2357 2754</p>	<p>Mumbai PwC House, Plot No. 18A, Guru Nanak Road - (Station Road), Bandra (West), Mumbai - 400 050 Phone +91-22 6689 1000</p>	<p>Gurgaon Building No. 10, Tower - C 17th & 18th Floor, DLF Cyber City, Gurgaon Haryana -122002 Phone : +91-124 330 6000</p>	<p>Pune GF-02, Tower C, Panchshil Tech Park, Don Bosco School Road, Yerwada, Pune - 411 006 Phone +91-20 4100 4444</p>	<p>For more information contact us at, pwctr.knowledgemanagement@in.pwc.com</p>

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