



SEBI's Mercy For Stressed Asset Transactions: The Rationale And Two Unanswered Questions

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Market regulator SEBI has decided to lend a helping hand to RBI in its effort to resolve the non-performing assets problem.

The Securities and Exchange Board of India on Wednesday decided to exempt acquirers of stressed assets, doing so under a Reserve Bank of India asset restructuring scheme, from the mandatory open offer requirement under SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011.

SEBI said, in a brief media statement, that relaxations from preferential issue requirements and from open offer obligations are available for lenders undertaking restructuring of listed companies in distress through the Strategic Debt Restructuring (SDR) scheme or any other such restructuring scheme under RBI guidelines.

“ It has been represented to SEBI that where the lenders have acquired shares and propose to divest the same to a new investor, they are facing difficulties as the new investor would need to make a mandatory open offer which would reduce the funds available for investment in the company.....it has been decided to extend the aforesaid relaxations to the new investors acquiring shares in distressed companies pursuant to such restructuring schemes.

SEBI Media Statement (June 21, 2017)

SEBI's exemption is accompanied by two conditions:

- Approval by the shareholders of the companies by special resolution and,
- Acquirer's shares to be locked in for a minimum period of three years.

The Rationale

Vyapak Desai, a partner at law firm Nishith Desai Associates said the provision of a special resolution maintains the rights of public shareholders in the absence of an exit opportunity via an open offer.

“ Ordinarily, a shareholder resolution would not have been required for such a transaction. But since the open offer requirement is being done away with, SEBI wants to be sure that the share sale to a new investor is something that the remaining shareholders are okay with.

Vyapak Desai, Partner, Nishith Desai Associates

SEBI's Takeover Regulations require that in matters of change in control or the acquisition of 25 percent or more equity, the acquirer must give existing public shareholders the opportunity to exit by tendering their shares in an open offer.

Kumar Saurabh Singh, a partner at law firm Khaitan & Co. told BloombergQuint that “shareholders should also get an opportunity to accept and approve this position as something which is in their interest”.

The First Unanswered Question

But who are these shareholders whose approval will be necessary via a special resolution? That's unclear at this stage.

A special resolution requires approval from at least 75 percent of the votes cast.

Singh pointed out that in most stressed assets cases, the lenders, by converting debt into equity, would've become the majority shareholders. If SEBI disallows these lenders from voting on the transaction on account of being a related party, the erstwhile promoters could end up with enough votes to block the transaction, he added.

Sumit Agrawal, a partner at law firm Suvan Law Advisors and former legal adviser at SEBI said that more clarity would emerge once the market regulator notifies the amendment.

“ As of today, there is no restriction unless there is a related party transaction. The Companies Act, 2013 doesn't envisage this situation where a new investor is coming in, what'll be the role of the promoter? SEBI's press statement doesn't answer the question at this stage.

Sumit Agrawal, Partner, Suvan Law Advisors

The Second Unanswered Question

SEBI's press statement is silent on the pricing mechanism that will apply to such stressed asset transactions. That is, can the sale of shares, by the lenders to the acquirer, be done at less than the prevailing market price? That may matter if, in anticipation of such an acquisition, there is a rise in the share price of the beleaguered company.