THE ECONOMIC TIMES

Sebi may set minimum contribution by PE promoters at 2.5% of fund corpus instead of 5%

Reena Zachariah, ET Bureau Apr 2, 2012, 12.48AM IST

Tags: Supreme Court | Securities & Exchange Board of India | sebi | private equ ty | PE promoters | MCX Stock Exchange | Bimal Jalan comm ttee

MUMBAI: The Securities &, or Sebi, may relax rules stipulating minimum contr bution by the sponsor or promoters in a private equity fund after hectic lobbying by the PE industry. New Sebi rules may peg the minimum contribution at 2.5% of the fund corpus as against 5% proposed earlier.

Globally, it is an established industry practice for a general partner or promoter to contribute a certain percentage to show commitment. Though not mandatory in most markets, the limited partners - investors who put money in private equity funds - typically negotiate on 1-2% of the fund size as general partner commitment depending on the corpus of the fund.

"The 5% (floor) proposed by Sebi was way too high and, in fact, could discourage many successful professionals from getting into this space, which would have resulted in reduced competition in favour of institutional general partners," said Siddharth Shah, partner, funds practice group, Nishith Desai Associates, which advises several private equity funds.

A minimum contr bution of 5% of the fund corpus is considered high by most people as many private equity funds are promoted by professionals whose capacity to raise large sums is limited.

For instance, many funds are promoted by private equity fund managers or senior professionals in the industry.

HIGH CONTRIBUTION PROVES A DETERRENT

While these professionals may be able to raise upwards of $50-100 million from outside depending upon their profile, status and expertise, they may find it difficult to fulfill a high minimum contribution criterion of, say, 5% of the fund corpus.

The regulator had unveiled rules for alternative investment funds, including dividing the sector into nine categories. The plan now is to have only four categories such as venture capital (which may include small and medium enterprise funds), private equity (covering private investment in public equity or PIPE funds), hedge funds and others (which may cover strategy funds).

"This over-categorisation could severely hamper the flexibility of funds which would generally straddle multiple strategies to provide higher absolute returns to investors. A rationalisation of these categories into few distinctly differentiated strategies would be a welcome move," said Shah of Nishith Desai Associates.

The new rules are likely to be approved after they are discussed at a meeting of the Sebi board on Monday, according to a person with knowledge of the issue.

The board is also expected to discuss the Bimal Jalan Committee report on market infrastructure institutions that had proposed capping profits of stock exchanges, discouraged their listing and sought separation of the commercial and regulatory aspects of bourses.

There has not been much progress on it due to the severe criticism the report drew from market participants.

One of the key proposals of the panel was that public utilities such as stock exchanges and depositories should not be allowed to make super-normal profits.

The report said these entities should earn only reasonable profits in line with the average earnings of the corporate sector in the country.

"The general feeling inside Sebi is that in various activities which are regulated by Sebi we should encourage competition," UK Sinha had told ET in May 2011 after taking over as the chief of the market regulator.

Although it is not part of the agenda for Monday's meeting, the Sebi board may also discuss the future course of action on the MCX Stock Exchange case, according to a person who was briefed on the proposals being considered for the meeting.

The Bombay High Court had told the regulator to take a decision on the application submitted by MCX-SX within a month.

There have been reports that Attorney General Ghulam E Vahanvati has advised the regulator to appeal against the high court order. The regulator will take into account the AG's views before taking a final decision on whether to appeal before the Supreme Court.

On March 15, the high court ruled in favour of MCX-SX by setting aside Sebi's order rejecting the exchange's application seeking permission to offer trading platforms for equities. Currently, MCX-SX is only allowed to offer trading in currency derivatives.

In 2010, the regulator had denied MCX-SX a licence as it was dissatisfied with the manner in which the promoters had reduced their stake to comply with the shareholding norms for stock exchanges.