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# India's Liberalized Regime for Indian Companies to List Overseas

*By Aditya Shukla and Ruchi Biyani, of Nishith Desai Associates, Mumbai.*

Faced with recent currency depreciation and criticism on account of policy inaction, the Indian government, by way of a circular issued by the Reserve Bank of India ("RBI") in November 2013, relaxed the rules governing the listing of shares of Indian companies in overseas markets by removing the mandate to list domestically prior to or simultaneously with such foreign listing.

This measure was apparently aimed at signaling the reform strain of the government as well as gaining the confidence and modifying the perception of the markets.

The reform, although a welcome development, may be limited in its practical impact, especially in light of the broader regulatory requirements, compliance requirements of foreign exchanges and costs associated with undertaking and maintaining a foreign listing, which are some of the issues that may hinder the ability and flexibility of Indian companies to tap foreign markets.

This article highlights some of the opportunities and challenges which Indian companies may face when listing in foreign markets.

## History of Overseas Listing of Indian Companies

In the years that followed the initiation of the economic reforms of 1991, the regulatory scheme devised in 1993 allowed Indian firms to list abroad through the issuance of depository receipts ("DRs") in foreign markets against the equity shares of such companies as the underlying of such DRs. There was no obligation on an Indian company to list prior to or simultaneously on the Indian markets. Some companies, particularly during the Internet boom of the late 1990s and early 2000s, utilized this avenue to achieve a foreign listing and raise capital abroad. Some of the companies that achieved a foreign listing under this regime included Sify Technologies, an Internet service provider, and Rediff, an Internet portal, which raised capital by listing on the U.S. markets in 1999 and 2000, respectively.

The regulatory regime was later amended in 2005, wherein Indian companies were restricted from raising capital through a foreign listing without achieving a prior or simultaneous domestic listing. Further, companies that had already achieved a foreign listing and were still not listed on the domestic markets were required to list upon achieving a profit in the subsequent financial years or within a period of three years from

such amendment, whichever was earlier. As a result of this amendment, domestic companies were not able to achieve a foreign listing without domestically listing in India.

In order to address this hindrance, the market devised certain structures wherein an offshore holding company of the Indian company was created and then the shares of such offshore holding company were listed on foreign markets, thus achieving a foreign listing without the need to list domestically. Some of the companies which utilized this route to raise capital from foreign markets were Genpact, a business process outsourcing company, and MakeMyTrip, a travel portal.

## Mechanism for Foreign Listing by Indian Companies

Indian companies proposing to list abroad generally achieve such listing by way of the issuance of DRs. Under the Foreign Currency Convertible Bonds and Ordinary Shares (Through Depository Receipt Mechanism) Scheme, 1993 ("Scheme"), an Indian company may become listed on foreign markets through the issuance of DRs in foreign markets with the company's equity shares as the underlying. A company may choose to issue DRs in U.S. markets, which are generally called American Depository Receipts ("ADRs"), or it may choose to issue DRs in any other global market, which are generally called Global Depository Receipts ("GDRs"). ADRs and GDRs are negotiable instruments issued by a depository bank in the foreign market, with the rupee denominated equity shares of the issuer as the underlying of such ADRs or GDRs, which underlying is held by a custodian bank in India. Prior to the amendment, unlisted Indian companies could not have issued ADRs or GDRs without a prior or simultaneous listing of their shares in India.

## Scope of the Current Amendment and the Strings Attached

The amendment has been introduced on a pilot basis for a period of two years. Companies will have to comply with certain conditions in order to be eligible to raise capital via the foreign listing route.

Some of the important conditions which have to be satisfied are as follows:

- Foreign listing should take place on an exchange which is in an International Organization of Securities Commissions ("IOSCO") or Financial Action Task Force ("FATF") compliant jurisdiction or such other jurisdiction with which the Indian securities market regulator, the Securities and Exchange Board of India ("SEBI"), has a bilateral agreement.

- Any issuance of ADRs/GDRs in a foreign market shall be subject to Foreign Direct Investment ("FDI") regulation, including in relation to the sectoral caps, entry route, minimum capitalization, pricing norms, *etc.*

- The Indian company will have to satisfy the disclosure requirements of SEBI, in addition to the disclosure requirements of the foreign stock exchange where it proposes to list.

- The capital raised abroad may be utilized for retiring outstanding overseas debt or for *bona fide* operations of the Indian company abroad, including for making acquisitions.

- In case the funds are not utilized within 15 days from such raising of capital, then such funds shall be repatriated to India to be parked with an Authorized Dealer Category 1 bank and shall be used only for eligible purposes.

- The Indian company will have to submit the return filed by it with the foreign stock exchange also with SEBI for the purpose of the Prevention of Money Laundering Act.

In addition to the above, the following conditions will also have to be satisfied in accordance with the regulatory requirements specified by the RBI:

- The pricing of such ADRs or GDRs to be issued to a person resident outside India shall be determined in accordance with the Scheme as prescribed under paragraph 6 of Schedule 1 of Notification No. FEMA 20 dated May 3, 2000, as amended from time to time.

- The number of underlying equity shares offered for the issuance of ADRs or GDRs to be kept with the local custodian shall be determined upfront and the ratio of ADRs or GDRs to equity shares shall be decided upfront based on applicable FDI pricing norms of equity shares of the unlisted company.

- The unlisted Indian company shall comply with the instructions on downstream investment as notified by the RBI from time to time.

## Analysis of the Amended Regulatory Scheme

The following are some of the factors which require consideration by Indian companies before raising capital through a foreign listing under the amended Scheme:

### Onerous Disclosure Requirements

The amended Scheme requires Indian companies proposing to list on foreign markets to adhere to two different disclosure requirements at the time of listing. Firstly, it requires Indian companies to adhere to the disclosure requirements of the foreign stock exchange on which they propose to list. Secondly, it requires not only submission of the offer document filed with the foreign stock exchange to be submitted to SEBI, but it also requires the unlisted Indian company to submit the disclosures in the form prescribed by SEBI.

This simultaneous requirement of adhering to the standards of two different regulatory regimes in the context of disclosure erodes any comparative advantage such foreign market might have had in terms of disclosure requirements. Further, such an additional regulatory compliance requirement adds to the costs and complexity in-

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volved in such a listing, and could act as a disincentive for such issuers to list on foreign markets.

### Compliance, Costs and Other Considerations

The rigors of compliance and the associated costs of achieving and maintaining a foreign listing are among the things Indian companies should consider when deciding to list abroad. Such companies will have to satisfy the initial listing criteria of the foreign exchange wherever they propose to list, *e.g.,* a foreign exchange may have eligibility criteria with respect to minimum operating history, minimum paid-up capital, or revenue or profit threshold, which may make it difficult for certain companies, especially early-stage companies, to take the plunge. Once a company crosses the first hurdle of satisfying the eligibility criteria of a stock exchange, it becomes involved in the more elaborate listing process. This process is not only time-consuming but also has costs associated with it in the form of fees and expenses. Once a successful listing is achieved, then costs in the form of annual fees to the stock exchange, as well as costs associated with making continuous disclosures and advisories for maintaining such listing, keep recurring. So, *e.g.,* the listing fee on an Indian stock exchange may be as low as U.S.$400, compared to 5,000 euros (U.S.$6,867) on the Luxembourg Stock Exchange or S$100,000 (U.S.$78,823) on the Singapore Stock Exchange, or some 24,000 pounds (U.S.$39,875) for listing depository receipts on the London Stock Exchange. The listing fee is only one of many considerations which a company contemplating listing will have to consider. In light of varied compliance requirements and recurring costs which vary from country to country, companies should analyze in detail the benefits accruing from a foreign listing against the costs associated with such foreign listing.

### Applicability of Pricing Guidelines

The Scheme requires Indian companies to comply with the pricing guidelines when listing on foreign markets. Such a regulatory requirement inhibits the freedom of the Indian company to price and offer its shares to a diverse group of prospective shareholders. Such a regulatory constraint on pricing may impact the demand for such issuance in foreign markets and invariably reduces the flexibility of companies. The policy approach in this regard should be to leave the pricing of the issuance to the board of the company to decide what is in the best interests of the company. The specialized knowledge and close association and awareness of the board with the affairs of the company make it a natural and logical forum to decide on the pricing vis-à-vis the regulator. A regulatorily mandated price therefore is likely to be a sub-optimal solution to a problem which could have been solved more optimally.

### Government to Specify Eligibility Criteria as to Which Companies May Raise Capital by Way of ADRs/GDRs

The RBI circular provides that the government may specify the eligibility criteria for unlisted companies that may raise capital via the ADR/GDR route. This leads to further confusion and ambiguity. Further, it is not clear as to what happens if a company starts preparing for an issuance and the government specifies certain criteria that the company does not fulfill. Does it mean that such company would have to abandon the issuance process and incur costs? Further, it is not clear what would happen to a company that became listed under this scheme and subsequently the government notified the eligibility criteria and such listed company did not qualify per the notified criteria. These are some of the questions with no clear answers under the current regulatory scheme.

### Regulatory Uncertainty

One of the concerns for unlisted Indian companies considering a foreign listing is that the regulatory regime may in future be revised to require them to list domestically after the initial pilot period of two years, as happened in the past in 2005. A step which the government could take in this regard to allay such concerns is to adopt consistency and predictability in its policy making approach in order to gain the confidence of the market, for the market to actually rely on government policy and act accordingly.

### Potential of Higher Liability in Certain Foreign Markets

Companies should also be aware that offering securities in certain markets may expose them to higher potential liability in case of misstatement in the prospectus. For example, a misstatement in a prospectus when the securities offering is made in the U.S. could result in a higher civil liability, which may include punitive damages as well. There may also be potential criminal liability emanating from such misstatement in the prospectus. Therefore, companies should carefully consider the advantages and disadvantages before deciding whether to undertake a foreign listing.

## The Way Ahead

The amended provision now makes it relatively less cumbersome for Indian companies to list on foreign markets, without the need to list through an offshore holding company structure. This should facilitate and encourage capital raising activity by Indian companies on global markets.

However, a cost-benefit analysis should be undertaken by such companies proposing to raise capital on global markets, particularly on the parameters of their eligibility, listing costs, recurring costs comprising annual exchange fees and compliance costs, and the comparative value they would derive from listing on a particular market.

Such an avenue to raise capital may be attractive for certain kinds of companies that may not find sufficient market appetite or sufficient depth in the domestic markets, or that operate in niche sectors. Companies operating in, *e.g.,* the nanotechnology space, biotechnology or other technology-driven fields may discover that the risk, opportunities and rewards associated with such companies find greater acceptance in certain foreign markets.

Such foreign markets may be receptive to the ideas, innovative products and solutions and provide capital and the premium such niche companies deserve, and which the domestic markets could not have offered. For such companies, the relaxation in the regulatory scheme governing the listing of unlisted Indian companies in foreign markets provides a real viable avenue to raise capital. Therefore, a company contemplating whether to list its securities domestically or in a foreign market should base its determination on circumstances specific to that company.

Further, Indian companies that had earlier attracted private equity/venture capital investment have faced some difficulty in providing exits to their investors via the domestic capital markets, due to the markets being not so resilient since the financial crisis, especially for initial public offerings. This relaxed regulatory scheme should now enable foreign listings for such companies to provide a possible additional avenue to facilitate exits for their existing investors.

This should be a good sign for the economy at large, as the capital that is freed up should recycle into new investments for other companies, enhancing economic activity and growth.

*The text of the RBI circular is available, in English, at http://op.bna.com/wdpr.nsf/r?Open=besi-9gmrpj.*

***Aditya Shukla and Ruchi Biyani are Associates with Nishith Desai Associates, Mumbai. They may be contacted at aditya.shukla@nishithdesai.com and ruchi.biyani@nishithdesai.com.***


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