Consultation Paper

Review of the 'NCDs along with warrants' as a staple product and as a segregated product, offered through Qualified Institutional Placement under SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018

1. **Objective**

1.1. The objective of this discussion paper is to seek comments / views from the public and market intermediaries on review of the 'NCDs along with warrants' as a stapled product offering or as a segregated product offering, through Qualified Institutional Placement (QIP) route under SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018 ('ICDR).

2. **Background**

2.1. SEBI in the past as an effort to provide a competitive product to the Foreign Currency Convertible Bonds (FCCB) instruments and to arrest the export of domestic capital market, explored alternate structures which would yield the same benefits to the issuer, SEBI, in consultation with market participants, explored alternate structures which would have same benefits and also enhance the suite of products from the investors' point of view.

2.2. Accordingly, SEBI in the year 2008, permitted a listed company to make a combined offering of 'Non-convertible Debentures (NCDs) along with warrants' through the QIP mechanism under SEBI (Disclosure and Investor Protection (DIP) Guidelines, 2000. This was also captured in the SEBI ICDR Regulations, 2009 & SEBI ICDR Regulations, 2018.

3. **Present regulatory framework**

3.1. The chapter VI of SEBI (ICDR) Regulations, 2018, inter alia, provide guidelines for QIP including for eligibility conditions, appointment of lead managers, placement document, pricing of securities, application and allotment of securities etc. in respect of eligible securities offered under QIP route.

Regulation 171(a) defines 'eligible securities' and the same is reproduced as under -

"Regulation 171 Definitions

For the purpose of this Chapter:

a) "eligible securities" include equity shares, <u>non-convertible debt instruments along with warrants</u> and convertible securities other than warrants;"

"Regulation 179 Application and Allotment:

(3) In a qualified institutions placement of non-convertible debt instrument along with warrants, an investor can subscribe to the combined offering of non-convertible debt instruments with warrants or to the individual securities, that is, either non- convertible debt instruments or warrants

3.2. Thus the above framework in 2008 allowed the offering to be either stapled or segregated.

3.3. Regulation 31 (2) of SEBI (Issue and Listing of Debt Securities) Regulations, 2008 ('SEBI ILDS Regulations'),

"In particular, and without prejudice to the generality of the foregoing power and provisions of these regulations, such orders or circulars may provide for all or any of the following matters, namely:

(a) Electronic issuances and other issue procedures including the procedure for price discovery;"

3.4. In conjunction with the above provisions, SEBI vide Circular no. CIR/IMD/DF1/48/2016 dated April 21, 2016, introduced Electronic Book Provider (EBP) mechanism, which streamlines procedures for issuance of debt securities (including NCDs) offering efficient and transparent price discovery mechanism.

4. **Need for review**

4.1. Present framework under ICDR allows that in a QIP of 'NCDs along with warrants', an investor can subscribe to the combined offering of NCD instrument with warrants or to the individual securities, that is, either NCD or warrants, depending on type of offering made by the issuer i.e. whether issuer has offered staple product (where warrants attached with NCDs) or segregated product (where NCDs and warrants can be subscribed separately).

4.2. Therefore, in case 'NCDs along with warrants' are offered as segregated product, it may technically be considered only as “simultaneous but unlinked” issuance since subscribers can subscribe to both or either of the instrument.

4.3. In case of issuance of NCDs under SEBI ILDS Regulations, the EBP offers issuers a large market of investors and thus has an advantage of an efficient and transparent price discovery mechanism thus lowering the cost of debt for issuers and consequently benefiting the shareholders of the issuer companies. This has brought transparency, and done away with the discretionary and bilateral allotment of debt to specific entities which the market was used to. Presently, listing of NCDs of Rs 200 crore or above in a year is possible only if such issuance is through EBP mechanism.

4.4. In contrast to the NCDs on EBP market, ‘NCDs along with warrants’ under SEBI ICDR Regulations allows the issuer facility of discretionary allotment which has the advantage of choosing who the issuer can allot warrant and consequently who the shareholder would be.

4.5. There are apprehensions that the product 'NCDs along with warrants' may be misused where issuers try to stay away from the EBP mechanism by issuing a tail warrant with NCDs to Qualified Institution Buyers (QIBs) under SEBI ICDR Regulations.

4.6. There is a thought process that the 'NCDs with warrants' with segregated allotment, where an investor can subscribe to the individual securities, that is, either NCDs or warrants, is no longer a hybrid instrument and thus deserves to be treated in terms of issuance in the respective regulations i.e. NCDs issuance should be on EBP only in terms of SEBI ILDS Regulations and warrants under SEBI ICDR Regulations.

4.7. Also, presently in terms of provisions under ICDR Regulations, 2018, warrants can also be issued including to the QIBs through IPO/FPO/Rights Issue and Preferential allotment route. Though, in case of IPO/FPO/Rights Issue warrants can only be issued if attached with specified security, whereas, in case of preferential allotment naked warrants can be issued including to the QIBs by the issuer company in terms of provisions of Chapter V of Preferential Issue under ICDR Regulations, 2018 (as per the existing provisions, preferential issue can be made to not more than 5 QIBs). Further, the tenure, pricing and upfront payment requirements for issuance of warrants under QIP, Preferential issue and IPO/FPO/Rights Issue are different.

5. Proposal

5.1. The matter was deliberated at the Primary market Advisory Committee (PMAC), which has recommended that SEBI may seek public comments on the following:

5.1.1. Discontinuing segregated offering of 'NCDs along with warrants' to QIBs through QIP mechanism under SEBI ICDR Regulations.

5.1.2. Stapled offering of 'NCDs along with warrants' to QIBs may be retained under SEBI ICDR Regulations, with ability to segregate the instruments after the issuance/allotment. However, to curtail misuse of the product by way of issuing a tail warrant with NCDs, a minimum threshold may be prescribed for warrant portion [say warrant portion should constitute minimum 40% of total issue size].

5.1.3. Allowing issuance of 'naked warrants' to QIBs through QIP mechanism under SEBI ICDR Regulations with guidelines on upfront payment, pricing and tenure of warrants.

6. **Public comments**

6.1. Considering the implications of the said matter on the market participants including issuer companies and investors, public comments are invited on the proposal at para 5 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 **"Review of the 'NCDs along with warrants' under QIP"**.

6.2. The comments may be sent by email to Shri Rajesh Dangeti, GM at rajeshkd@sebi.gov.in and Shri Ankur Bishnoi, AGM at ankurb@sebi.gov.in or sent by post at the following address latest by December 17, 2020:

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Issued on: **December 02, 2020**