"Review of SEBI (DIP) Guidelines 2000- Proposals - Series V "

"Recommendations and Suggestions made by the Primary Market Advisory Committee (PMAC)"

[Comments on the recommendations and suggestions may be sent to the Corporation Finance Department, Division of Issues & Listing, SEBI or emailed to Ms.Usha Rangarajan, Manager @ ushar@sebi.gov.in, Mr Santanu Nath Bhaumik, Manager, at santanunb@sebi.gov.in or Ms. Neelam Bhardwaj, DGM, at neelamb@sebi.gov.in or faxed to 91-22-22045633 on or before September 12, 2003]

1. The PMAC at its last meeting, considered several issues placed before it and has made recommendations /suggestions to SEBI on the following two issues :

Recommendations/Suggestions of Primary Market Advisory Committee

1. Use of Shelf Prospectus facilities in the issue process

Sec. 60A of The Companies Act 1956 deals with the provisions pertaining to Shelf Prospectus. Shelf prospectus is defined as a prospectus issued by any financial institution or bank for one or more issues of the securities or class of securities specified in that prospectus. As per Section 60A(1) of Companies Act, any public financial institution, public sector banks or schedule bank whose main object is financing shall file a shelf prospectus. There is no explicit provision in SEBI (DIP) Guidelines, 2000 regarding shelf prospectus. The issue considered was whether DIP Guidelines may be amended to extend the facility of shelf prospectus.

The Committee recommended that shelf prospectus facility may be extended to public sector banks and scheduled banks along-with public financial institutions for issuance of debt instruments. However the committee felt that it is not advisable to extend the shelf prospectus facility for issue of equities. The committee also recommended that shelf prospectus facility may be extended to subordinate debt issues of banks.

2. Review of DIP Guidelines for Preferential Issues (Chapter XIII of DIP Guidelines)

a Fixing of cap price

SEBI has received representations that in the absence of cap price, companies issue shares at an exorbitantly high price. This high price thereafter acts as a benchmark price in the market and triggers speculative trading in many cases.

The committee noted that the existing guidelines have provided only for a floor price. The members deliberated on the issue and recommended that fixation of cap price is not the solution. The decision should be left to both the parties concerned, i.e. the company and the allottee, particularly because the preferential allotment is made to a select group of people and not to the public in general.

b. Special Resolution through postal ballot

A company can make preferential allotment by passing a resolution in general body meeting under Section 81(1A) of Companies Act, 1956. The committee agreed that, in many cases, general meeting, for passing resolution approving preferential allotment, is held at remote places, as a result of which common shareholders cannot attend the meeting and the resolution gets passed without their participation. The committee recommended that special resolution through postal ballot may be made mandatory for Preferential Issues.

c. Status of non-compliant shares

The Committee observed that there are cases where companies have allotted shares through preferential allotment, but exchanges have not given permission for listing of those shares on account of non compliance of guidelines. Thus the shares remain allotted and not listed. The Committee suggested the following measures to deal with the issue of non compliant shares

SEBI may take up with DCA to stipulate that the preferential allotment made by a listed company should be considered void-ab-initio if Stock exchanges do not grant listing permission to these shares. SEBI may also consider appointing merchant bankers to ensure due diligence and avoid non compliances in future

d. Possible manipulation of price to "fix" the preferential issue

As regards price manipulation, both upward and downward, the members were of the view that guidelines cannot address such issues and recommended that it can be addressed only through strict monitoring and surveillance by SEBI.

e. Non-receipt of funds in lieu of the shares allotted

As on date, there is no requirement for the companies to keep the consideration received for allotment of shares on preferential basis in a separate account till allotment of the shares. SEBI has received several representations from exchanges where they have expressed their apprehensions that the company has not received any money from the allottees and the consideration shown to the exchanges, as received from the allottees is only book entry/circular entry.

The members deliberated on the various options to address the concern of non serious/fraudulent allottees of shares on preferential basis. While doing so, members drew a parallel between preferential allotment and public issues and suggested the following options:

a. The proposed allottees, have to bring in the funds prior to the date of general meeting. This will ensure that only serious investor will take part in preferential allotment. The funds can be kept in an escrow account.

b. The committee felt that the time period for allotment for shares issued preferentially may also be reduced, say to 1 month (from existing 3 months) as even in case of public issues, despite the various formalities to be completed, the period for allotment of shares is 30 days.

f. Issue of shares on swap basis through preferential allotment

SEBI has received several representations from stock exchanges regarding their apprehensions about the valuations of the companies being acquired or to whom shares are being issued on a share swap basis, particularly in view of the fact that there is no lock-in requirement for shares issued on stock swap basis. The committed deliberated on the misuse of shares on swap basis, particularly in view of the fact that there is no lock-in requirement for shares issued on stock swap basis. The Committee recommended that shares allotted on preferential basis involving swap of equity shares/ securities convertible into equity shares at a later date, for acquisition, should not be exempted from lock-in requirement. The committee also opined that SEBI may consider prohibiting issuance of shares through preferential allotment for consideration other than cash.

The members advised that as the recommendations/suggestions pertaining to various aspects of preferential allotment (as elaborated above) are far reaching, they may be put up on the website for public comments.