<u>Subject - Review of the existing framework for Offer for Sale (OFS) of shares through Stock Exchange Mechanism.</u>

1. Objective

1.1 The objective of this memorandum is to propose modifications to the existing OFS Framework so as to bring in more flexibility and efficiency in the framework.

2. Background

2.1 OFS through stock exchange mechanism was introduced by SEBI in February 2012, to enable divestment by promoters to achieve minimum public shareholding in listed companies. Since then, the provisions have undergone many changes. The last significant modification was done in December 2018.

2.2 The existing provisions of the OFS framework proposed for modification are highlighted below:

2.2.1 The OFS mechanism is available for companies with market capitalization of INR1,000 Cr. and above ("eligible companies"). The size of the offer has to be a minimum of INR 25 Cr. However, size of offer can be less than INR 25 Cr. so as to achieve minimum public shareholding in a single tranche. For any non-promoter shareholder of the eligible companies, to offer shares through the OFS mechanism, their holding should at least be 10% of share capital.

2.2.2 The promoter(s)/ promoter group entities and the non-promoter shareholder (together called as "sellers") of the eligible companies should not have purchased and/or sold the shares of the company in the 12 weeks' period prior to the offer and they should undertake not to purchase and/or sell shares of the company in the 12 weeks period after the offer. However, within the cooling off period of +12 weeks, the promoter(s)/promoter group entities can offer their shares only through OFS/ Qualified Institution Placements (QIP) with a gap of 2 weeks between successive offers.

2.2.3 Any unsubscribed portion of retail category after allotment shall be eligible for allocation in the non-retail category.

2.2.4 Seller(s) shall announce intention of sale of shares along with relevant details latest by 5 pm on T-1 day (T day being the day of the OFS) to the stock exchange. Stock exchanges shall inform the market immediately upon receipt of notice.

2.2.5 No single bidder other than mutual funds and insurance companies shall be allocated more than 25% of the size of OFS.

2.2.6 Currently, the framework does not provide for sale of units of REITs/ InvITs through OFS mechanism by sponsors/ sponsor group entities and other unit holders.

2.3 Utilisation of the OFS Mechanism

2.3.1 (This has been excised for reasons of confidentiality.)

2.3.2 (This has been excised for reasons of confidentiality.)

3. Deliberations in Secondary Market Advisory Committee (SMAC)

3.1 Based on the feedback received from various stakeholders, SEBI had constituted a Working Group (WG) of Stock Exchanges (NSE, BSE & MSEI) to suggest changes, if any, to the existing OFS Framework. Based on the recommendations of the WG and subsequent internal deliberations, the proposals were discussed in Secondary Market Advisory Committee (SMAC) in its meeting held on July 26, 2022. The Committee deliberated on the matter and recommended the followings:

3.1.1 **Relaxation in the existing minimum shareholding norms for non-promoter shareholder for OFS:** Currently, OFS can be used by promoter(s)/ promoter group entities and non-promoter shareholders subject to certain conditions. Non-promoter shareholders who hold at least 10% of the share capital of any eligible company and are willing to sell at least shares of INR 25 Cr. and more are eligible to offer their shares through OFS mechanism. Thus, for example, if a non-promoter shareholder holds 5% of the share capital of an eligible company and the value of his holding is INR 100 Cr., she/he cannot offer shares through OFS mechanism. On the other hand, if a non-promoter shareholder who holds 10% share capital of another eligible company whose market value is of INR 30 Cr. can offer the shares of INR 25 Cr. or more through OFS. Thus an inconsistency is observed as a non-promoter meeting the value threshold may not be able to use the OFS mechanism unless she/he also meets the shareholding percentage threshold. The requirement relating to Minimum offer size is more substantive than the minimum shareholding percentage since the guiding principle of OFS is that large order should not distort the market/price discovery mechanism. Accordingly, SMAC has recommended that the existing requirement of 10% shareholding for the non-promoter shareholder to offer their shares through OFS mechanism may be done away with.

Proposal: Recommendation of SMAC may be accepted.

3.1.2 **Cooling Off Period:** A cooling off period of (+-) 12 weeks has been provided to the sellers of eligible companies for availing OFS mechanism. This puts a bar on sellers from buying/selling shares during the cooling off period. For a very liquid stock having minimal market impact, the existing cooling off period requirement may not be appropriate. In this regard, the existing requirement for cooling off period was reviewed both in terms of the timelines and eligible companies based on the liquidity and impact cost. Accordingly, SMAC has recommended that eligible companies may be classified into the following three categories along with respective cooling off period for before and after OFS:

i. "Most Liquid Stocks" are those stocks that have impact cost of up to 5 basis point for a trade of Rs. 1 Lakh. – Cooling off period of +-1 week.

ii. “Liquid Stocks” are those having impact cost of more than 5 basis points and upto 10 basis point for a trade of Rs. 1 Lakh. - Cooling off period of +-2 weeks; and

iii. “Illiquid Stocks” are stocks having impact cost of greater than 10 basis point - Cooling off Period of +-4 weeks.

The impact cost will be calculated on the basis of trading in last 6 months prior to the month in which OFS papers are filed with the stock exchange.

As per the data provided by NSE, there are over 900 companies that are eligible for OFS. By the above yardstick around 180 companies can be categorized as “Most Liquid”, 290 companies are “Liquid” and rest all eligible companies are “Illiquid”.

Further, it is proposed that, in case of under subscription in the original OFS which was made for MPS compliance, promoter(s)/ promoter group entities may be allowed to offer the unsubscribed portion of OFS in the open market with a gap of 2 weeks from the closure of OFS. In this regard, it is mentioned that in one of the instance, exemption from the existing +12 weeks’ clause has already been granted to carry out sale transaction through other methods after it has failed to comply with MPS requirement despite multiple OFS.

Proposal: Recommendation of SMAC may be accepted.

3.1.3 **Enabling allocation of unsubscribed portion of the non-retail segment to retail segment:** While the OFS mechanism was successfully used to divest the stake by the seller, an examination of participation by investors in the recent issues of OFS showed that retail participation has always been lagging behind the non-retail bids in terms of number of times subscribed. The current provisions allow non-retail to carry forward their bids to the retail segment in case there is not much interest in retail segment. However, retail investors are, at present, not allowed to participate in the unsubscribed portion in the non-retail segment.

Since the shares of the eligible company is already listed and traded, information about the company is publicly available to all investors including the retail investors. Further, as per the existing requirement the floor price for the retail segment, in case of under subscription by the non-retail segment, will be the initial floor price set in the OFS for non-retail segment. Hence, in the light of no adverse implications, SMAC has recommended to make a level playing field for both retail and non-retail by allowing unsubscribed portion of non-retail segment to be subscribed by the retail investors.

Proposal: Recommendation of SMAC may be accepted.

3.1.4 **Notification by the seller to Stock Exchanges:** The Seller shall notify to the stock exchanges its intention for sale of shares latest by 5 pm on T-1 day (T day being the day of the OFS). Considering the difficulties faced by the merchant bankers, sellers in foreign jurisdiction, etc. and it is noted that in the past, at times extension was granted beyond 5 p.m. in case of OFS by the Government of India/ PSUs since it involves approvals from various offices. Accordingly, SMAC has recommended that stock exchanges may be empowered to allow extension in notice of OFS on T-1 day till 6 p.m., on case-to-case basis, subject to properly recording the reason for granting such extension.

Proposal: Recommendation of SMAC may be accepted.

3.1.5 **Relaxation in the restriction of 25% allocation to single bidder other than mutual funds and insurance companies, in case of companies which are MPS compliant:** The OFS mechanism provides for allocation of more than 25% of shares only to mutual funds and insurance companies. In case of MPS non-complaint companies, the provision of allocation of more than 25% of shares only to mutual funds and insurance companies may facilitate wider public shareholding to meet MPS requirements. However, for a company that is already compliant with MPS norms the restriction on allotment acts as artificial barrier and affects efficient price discovery. This may also have impact on the overall offer as in the case of OFS, the seller is diluting his/her stake in the company which is already listed and information in respect of the security is already available in the public domain and hence the allotment shall be on the price-priority basis without restricting the amount of allotment. Thus, to make the market more competitive and efficient, SMAC has recommended that for the companies which are MPS compliant, the restriction of 25% allocation to single bidder may be removed. For the OFS of companies which are non-compliant with MPS norms, such restriction may continue to facilitate wider public shareholding.

Proposal: As the existing limit for single bidder at 25% other than mutual funds and insurance companies is reasonably high and relaxation as recommended by SMAC on the said limit may increase concentration with single bidder other than mutual funds and insurance companies, which may not be desirable, it is proposed that the recommendation of SMAC may not be accepted.

3.1.6 **Enabling OFS mechanism for sale of listed units of REITs/InvITs:** Currently, there is no provision for sale of units of REITs/ InvITs through OFS mechanism by sponsors/ sponsor group entities and other unit holders. Introduction of an OFS framework for REITs and InvITs will help the sponsor and sponsor group and other unit holders to effectively dilute their stake with greater flexibility in pricing the units in transparent manner and with wider participation. Also the OFS mechanism is expected to enable wider distribution of units, better liquidity and depth of REITs and InvITs market. Additionally, REITs/InvITs are also required to comply with minimum public unitholding norms, an OFS framework would serve as a viable avenue through which such compliance may be achieved. In this regard, SMAC has recommended to allow sellers of listed REIT/ InvIT to offer their holdings through the OFS mechanism.

Proposal: Recommendation of SMAC may be accepted.

4. Proposal

4.1 In view of the above and based on the recommendations of SMAC, the following proposals are placed before the Board for consideration and approval:

4.1.1 The existing requirement for a non-promoter shareholder to hold at least 10% of the share capital of the eligible company to offer their shares through OFS mechanism may be done away with.

4.1.2 For the purpose of cooling off period before and after OFS, the eligible companies may be classified into three categories based on liquidity. The cooling off period for such categories of eligible companies may be as under:

i. "Most Liquid Stocks" are those stocks that have impact cost of up to 5 basis point for a lot size trade of Rs. 1 Lakh. – Cooling off period of +-1 week.
ii. "Liquid Stocks" are those having impact cost of more than 5 basis points and upto 10 basis point for a lot size trade of Rs. 1 Lakh. – Cooling off period of +-2 weeks and
iii. "Illiquid Stocks" are stocks having impact cost of greater than 10 basis point a lot size trade – Cooling off period of +-4 weeks.

However, in case of under subscription of a company (whose shares are illiquid), if the original OFS is made for MPS compliance, promoter(s)/ promoter group entities may be allowed to offer the unsubscribed portion of OFS in the open market with a gap of only 2 weeks from the closure of OFS.

4.1.3 In addition to the quota for the retail segment, retail investors may also be allowed to bid for the unsubscribed portion of non-retail segment.

4.1.4 The existing requirement that the seller(s) shall notify to the stock exchanges its intention for sale of shares latest by 5 pm on T-1 day (T day being the day of the OFS) may be continued. However, stock exchanges may be allowed to grant extension to the seller(s) for the notice of OFS on T-1 day till 6 p.m., on case-to-case basis, subject to properly recording the reason for granting such extension.

4.1.5 OFS mechanism may be made available to listed REIT/ InvIT unit holders/Sellers to offer their holdings.

4.2 The detailed guidelines on the revised OFS mechanism may be issued by way of a circular.

5. The Board is requested to consider and approve the proposals given at para 4.1 above and authorize the Chairperson to take consequential and incidental steps to give effect to the decisions of the Board and also to carry out any future modifications in the OFS mechanism.

Annexure-A

This has been excised for reasons of confidentiality.