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Delisting of Securities

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New Rule 21 of SCR Rules 1951 as well as the Regulations issued by the SEBI seek to govern delisting of shares. However, SCR Rules seem to run in conflict with SEBI Regulations and suffer from incongruities. As this would not be desirable there is an urgent need to address this.

A company intending to offer securities to public and raise resources is required to list such securities in one or more recognized Stock Exchanges to provide ready liquidity and a platform for price discovery to investors. Having so raised resources from the general public, a listed company is subject to rigorous reporting and disclosure requirements. Business by nature involves change. A company or its promoters may like to opt out of public funding and lay emphasis on greater flexibility and minimal disclosure by reorganising their business. Delisting of securities comes as a useful tool under these circumstances. Such delisting doubtless has to be accomplished with utmost comfort as protection to the outstanding public investors. Regulations and Guidelines for delisting seek to fulfill these objectives.

Fresh Regulations on Delisting

Section 21A was introduced in the Securities Contracts (Regulation) Act, 1956 (SCR Act) effective 12-10-2004. It permitted recognized Stock Exchanges to delist securities on any of the ground or grounds as may be prescribed in this Act. An aggrieved company or investor has right of appeal before the Securities Appellate Tribunal.

In furtherance of the above, Rule 21 has now come to be inserted in the Securities Contracts (Regulation) Rules, 1957 (SCR Rules). It deals with delisting compulsorily inflicted by stock exchange as well as voluntary delisting initiated by a company.

Simultaneously SEBI has issued the Securities and Exchange Board of India (Delisting of Equity Shares) Regulations, 2009 (SEBI Regulations) on 10-06-2009. They would prospectively operate in place of erstwhile SEBI (Delisting of Securities) Guidelines, 2003.

Both SCR Rules and SEBI Guidelines on delisting have been notified on the same day namely 10-06-2009. They deal with

the same subject towards regulating delisting and protecting public shareholder. The duplicity of regulations and the dichotomy of provisions inherently inconsistent with each other could have better been avoided. In particular, SCR Rules would seem to run in conflict with SEBI Regulations and suffer much from deficiencies and incongruities in dealing with the issue on hand.

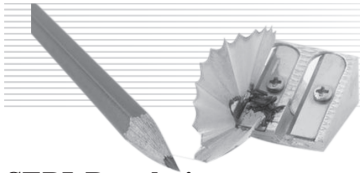
Securities Contracts (Regulation) Rules

A comprehensive list of disqualifications has been conceived to trigger compulsory delisting by Stock Exchanges. A stock exchange is authorized to delist the securities in accordance with the regulations made by SEBI on following grounds:

- Losses suffered by listed entity during the preceding three consecutive years leading to negative networth
- Suspension of trading in the securities for more than 6 months
- Infrequent trading in the securities during the preceding 3 years
- Conviction of company, its promoters or directors for violation of SEBI Act, Depository Act and related Rules and Regulations leading to imposition of penalty of more than Rs.one crore or imprisonment for more than 3 years
- Non traceability of company, its promoters or directors
- Fall in public shareholding to below minimum threshold level

Voluntary delisting can be permitted by Stock Exchanges subject to following conditions:

- Minimum period of 3 years of listing
- Approval of delisting by two-thirds of public shareholders
- Exit option to public shareholders except when listing continues in NSE/ BSE



SEBI Regulations

The SEBI Regulations also deal with both voluntary and compulsory delisting. It offers exit opportunity except when listing continues in NSE or BSE. It provides for fair price determination for exiting shareholders and payment security for them.

Even in the case of compulsory delisting by Stock Exchanges, rights of public shareholders are sought to be protected by mandating the promoter to acquire the delisted shares by paying them the value determined by the valuer, subject to their option of retaining their shares. Further the company, its whole-time directors, its promoters and companies which are promoted by any of them shall not directly or indirectly access the securities market or seek listing for any equity shares for a period of 10 years from the date of such delisting.

Responsibility to protect public shareholder

The genesis of company as a form of business entity stems from limited liability concept. A company is distinct and separate from the persons associated therewith. Such a corporate veil can be lifted only in certain events like frauds and misdeeds of persons owning or controlling its operations.

Recent exceptions to the above gospel were after the advent of SEBI and its imposing certain obligations on promoters and their associates. Such a trigger arises in the event of change in substantial ownership or management [SEBI (Substantial Acquisition of Shares and Takeover) Regulations, 1997] and also in the case of delisting of securities. Relevant SEBI Guidelines stipulate the need for mandatory public offer and acquisition of public shareholding at a fair price. Such a prescription is of course understandable and also well justified to protect the interest of public shareholder.

SCR Rules – Rule 21(2)(b) and Rule 21(3)(c) - however make every company, promoter and director to be jointly or severally liable to purchase the outstanding securities from those holders who wish to sell them at SEBI formula price. It is strange that every director, be it an independent or professional director, is included in the list of persons responsible for protecting public shareholder through such acquisition.

In fact, a company cannot purchase its own shares from the shareholders that would expressly violate Section 100 of the Companies Act, 1956. This can be done only with the approval of Court. Thus the requirement of Rule 21 of SCR Rules clearly runs contrary to the Companies Act and to that extent is patently void.

On the contrary, SEBI Regulation imposes such an obligation only on the promoters that would seem both pragmatic and equitable.

Delisting from all stock exchanges

Rule 21(2) of the SCR Rules catalogues the consequences of compulsory delisting. Clause (b) of this Rule prescribes that when once the securities of a company are delisted by one stock exchange, they shall be delisted from all recognized stock exchanges.

This stipulation though well intended is impracticable. It is likely that the securities of a company may be infrequently traded in one stock exchange but it might have regular trading in other exchanges. Hence compulsory delisting in one exchange cannot *ipso facto* lead to delisting from all stock exchanges. At best this shall be confined to cases of fraud or vanishing company or its promoters.

Further at present there is no mechanism available for effective exchange of information between stock exchanges. An earlier attempt to have a Central Listing Authority could not succeed leading to the repeal of SEBI (Central Listing Authority) Regulations 2003. The salutatory provision in Regulation 22(6)(b) of SEBI Regulations may not suffice to trigger unified and coordinated action by all Stock Exchanges.

Approval for voluntary delisting

Rule 21(3) of SCR Rules deals with voluntary delisting on the request of a listed company. This however calls for the approval of such a proposal by the two-thirds majority of public shareholders.

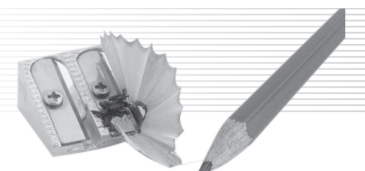
The Companies Act, 1956 contemplates two types of resolutions, namely, ordinary and special. While the former is passed with simple majority, a special resolution requires three-fourth majority. All the businesses of a company are dealt with only through ordinary or special resolution. One notable exception of course is the approval for a Scheme of Arrangement or Compromise under Section 391 that not only requires three-fourth in value but also a simple majority in number of shareholders or creditors attending the relevant meeting.

It looks therefore strange that for the first time a different kind of majority, namely, two-third is being prescribed under the new SCR Rules. For both uniformity and consistency, there shall not be too much variance or tinkering in imposing the criterion to decide upon requisite majority.

While the requisite resolution shall be approved by two-third of public shareholders, neither SCR Act nor SCR Rules define the term 'public shareholder'. This term is defined only in SEBI Regulations. While SEBI Regulations borrow the definitions in SCR Act or SCR Rules, the *vice versa* is rather conspicuous by its absence.

Curiously, Rule 19(2)(b) of SCR Rules prescribing minimum

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public holding in a listed entity excludes the holdings of Central or State Government, their Agencies and Public Financial Institutions from the scope of public shareholder. Logically their shareholding cannot in the event of delisting be treated as non public shareholding.

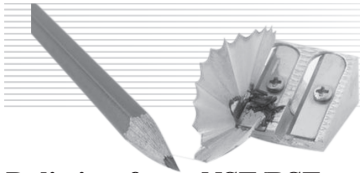
In fact the concept of interested directors and their exclusion for the purpose of quorum and voting rights is presently confined only to a Board meeting in the Companies Act. All shareholders, whether interested or disinterested, are entitled to their respective share of votes in a general meeting with the only rider that disclosure of interest is given in the explanatory statement. The departure from this tenet is of course unexceptionable to protect public shareholder.

The relevant provision in SCR Rules is however ambiguous as it requires the approval by two-third of public shareholders. It fails to clearly state whether such an approval is by way of number or value of public shareholders. It is equally vague whether the two-third majority must represent the entire population of public shareholders or only those participating in the voting. SEBI provisions on the other hand are clear and unequivocal on this.

Comparative provisions of SCR Rules and SEBI Delisting Regulations

SCR Rules and SEBI Delisting Regulations operate in the same field and are overlapping and conflicting in many provisions. A comparison of broad features is made hereunder.

<i>Description</i>	<i>SCR Rule</i>	<i>SEBI Guidelines</i>
Protection of public shareholders in case of compulsory or voluntary delisting	Company, promoter and director are jointly and severally liable to purchase the outstanding securities.	Only promoter is liable to purchase shares.
Persons eligible for exit option	All the holders who wish to sell at fair price	Only public shareholders
Approval for voluntary delisting from one or more SE on continuing listing with either NSE or BSE	No separate procedure – Approval required by the two-third of public shareholders.	Approval by a resolution of Board of Directors in its meeting
Approval for voluntary delisting from one or more SE without presence in NSE or BSE	By the two-third of public shareholders	(i) Prior approval of Board of Directors in its meeting. (ii) Prior approval of shareholders by special resolution passed through postal ballot. (iii) Above special resolution further requires two-third consent of public shareholders.
Passing of resolution by shareholders	No special resolution is insisted	Special resolution shall be passed through postal ballot.
Voting by public shareholders	Approval shall be by two-third of public shareholders – whether this is by number or value is left vague – Also whether two-third of public shareholder or only those voting must approve is unclear.	Provisions clearly spelt – The two-third majority shall be in terms of votes cast in favour of resolution thereby meaning two-third majority by value and representing those voting.
Definition of promoter and public shareholding	No definition – No reference of SEBI Act or Regulation – Rule 19(2)(b) excludes Government/ Institutional shareholding from the scope of public shareholding	Promoter and public shareholding clearly defined.
Compulsory delisting	Compulsory delisting by one exchange would lead to delisting from all other stock exchanges	No such provision – Only intimation by delisting exchange to other exchanges



Delisting from NSE/BSE

SEBI Delisting Regulations, 2009 do not explicitly bar a company delisting its securities from NSE/ BSE to continue with its listing in other stock exchanges. The only condition for doing so is to offer an exit option to public shareholders. This however runs contrary to SEBI's policy to insist upon mandatory listing in NSE/ BSE.

Press Release No.192/ 2009 dt.18-06-2009 conveys the decision of SEBI Board meeting towards listing of IPOs on Stock Exchange with nationwide trading terminals. Henceforth an unlisted company making IPO shall list the securities on at least one stock exchange having nationwide trading terminals. This is with a view to provide adequate

liquidity and trading platform to investors in the securities of the company.

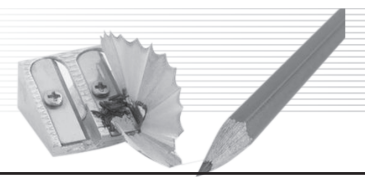
No company so far appears to have exited NSE/ BSE and persists with listing only in regional stock exchanges. However such a possibility does exist and hence SEBI Delisting Guidelines shall explicitly bar same to align with its latest policy decision towards mandatory listing of IPOs in NSE/ BSE.

Old SEBI Guidelines v. New Regulations

The new Regulations of SEBI are doubtless more comprehensive and they overcome some of the inadequacies of old Guidelines. A broad comparison of the two is made hereunder.

Sl. No.	Description	SEBI Delisting Guidelines, 2003	SEBI Delisting Regulations, 2009
1	Types of Delisting	(i) Voluntary delisting by promoters (ii) M&A/Scheme/Arrangement reducing Public shareholding below minimum limit (iii) Consolidation of shareholding by persons in control of management (iv) Compulsory delisting by SEs	(i) Voluntary delisting by company (ii) Compulsory delisting by SEs
2	Minimum Listing period for Voluntary Delisting	Three years on any Exchange	Normally three years. Not applicable when after delisting, shares remain listed in NSE/ BSE
3	Approval for Voluntary Delisting	By shareholders through Special Resolution passed at General Meeting	(i) Board Resolution where no exit option is required. (ii) Board approval plus Special Resolution of shareholders passed through postal ballot in other cases (iii) Additional condition that such Special Resolution shall have the support of two-third majority of public shareholders
4	Approval of SEs	Single stage approval	(i) Single stage approval where no exit option is required. (ii) In other cases, two-stage approval – First in principle and then final approval
5	Time limit for SE approval	Nil	30 working days from the date of receipt of Application complete in all respects
6	Appointment of professionals	Merchant Bankers to be appointed	In addition other intermediaries as are considered necessary shall be appointed
7	Record Date to determine	No explicit provision	Public announcement to state 'specified date'

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Sl. No.	Description	SEBI Delisting Guidelines, 2003	SEBI Delisting Regulations, 2009
	eligible Public Shareholders		for this purpose that shall be within 30 working days of public announcement
8	Payment Security	No explicit mention of escrow account and conditions therefor, excepting broad mention in Schedule I & II	Regulation 11 contains detailed prescription of escrow account
9	Letter of Offer	No specific prescription	Detailed prescription under Regulation 12
10	Holders of Depository Receipt	No specific reference	Specifically excluded from public offer
11	Minimum Shares to be acquired from Public	To raise minimum public holding to threshold level	Additional criteria of acquiring 50% or more of offer size
12	Rights of remaining shareholders	Tender securities at the same price during further 6 months period from delisting	Time limit extended to one year from the date of delisting
13	Consequences of Compulsory Delisting	Nil except exit option for public shareholders	Additionally, the company, its wholetime directors, its promoters and the companies promoted by any of them are denied access to securities market for 10 years.
14	Delisting by small companies and by operation of Law	No special provisions	Simplified procedure introduced under Chapter VII.
15	Relisting of Delisted Securities	Uniform waiting period of 2 years	Varying waiting period of 5 – 10 years.

Transitional Provisions

Regulation 31 deals with transitional provisions. Where a company has initiated steps for delisting or an application for delisting is pending with SEs, it shall be covered by the provisions of old Guidelines. Even where an exit opportunity is completed or an exit opportunity has been initiated but not completed, the remaining procedures will have to be complied with under the old Guidelines.

The new Regulation contains a time limit of one year from the date of passing Special Resolution by shareholders to make the final application to the concerned SEs. On the contrary, there was an open ended time limit for such Special Resolution under the Guidelines. This gave rise to a spate of queries from various market participants to SEBI for clarification.

Responding to the above, SEBI has now clarified on 14.09.2009 on the interpretation of Transitional Provisions. Only where the Special Resolution of members has been acted upon within a period of three months from the date of the clarificatory circular, old Guidelines would apply. For this

purpose, the activities to implement includes the opening of the book building process in the determination of exit price. Otherwise, the company would come under the new Regulation and it has to pass a fresh Special Resolution of members to proceed with delisting.

Conclusion

The new set of delisting provisions have come to strengthen the interest of public shareholders, while simultaneously facilitating the promoters' objective to have greater control and flexibility of operations. It however looks odd and odious to have two different pieces of legislations dealing with the same subject matter. Since SEBI has been given the task of market regulator and responsibility to protect common investor, the delisting regulations shall be under the sole domain of SEBI. The discernible disconnect and dissonance between SCR Rules and SEBI Regulations may lead to avoidable complications and defeat the underlying objectives. Hence the operating part of new Rule 21 of SCR Rules would merit annulment at once. □