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'Promoter' PEs won't have it easy anymore

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MUMBAI: The Securities and Exchange Board of India's (SEBI) recent move, modifying the definition of a 'promoter' under the Issue of Capital and Disclosure Requirements (ICDR) regulations, is likely to have a major bearing on companies with private equity investors, according to investment bankers.

The ICDR regulations, issued in late August, have expanded the definition of a promoter to include a person or persons who are in 'control' of the issuer. The term 'control' has been defined according to the takeover code, which means the right to appoint majority of the directors or the right to control the management or policy decisions. Private equity investors often insist on these rights at the time of investing in an unlisted company.

"The change in definition of promoter could have implications for companies with private equity investors," says Mehul Savla, director, RippleWave Equity.

"While most special rights fall away on listing, as companies need to amend their Articles as per listing agreement norms, PE investors with certain continuing rights may fall within the purview of "persons in control" of the issuer," he says. Merchant bankers say the agreement conferring special rights on PE investors is between the promoter and the PE investor, and not between the company and the PE investor. So, even after the articles of the company are amended post-listing, the earlier agreement between the promoter and the PE investor remains.

But with the new definition of 'promoter' in place, private equity investors with special rights will have to play a more active role in the functioning of the company, and will also be subject to the disclosure requirements applicable to promoters. This is something that most private equity investors are averse to. Likewise, the new disclosure and investor protection regulations have also tweaked the law with regard to group company disclosures, process of due diligence, besides requiring public comments on the draft offer document.

The new regulations now require that the draft offer document filed with the regulator to be made public for comments for a period of 21 days. After addressing the comments received in the offer document, lead managers will have to submit a status report to SEBI after the expiry of the 21-day period. Although merchant bankers say the public comment process on the draft prospectus always existed. It's just that SEBI has now put it in 'black and white'.

Before SEBI's rule tweak, the draft offer documents were only required to be filed with SEBI for the purpose of receiving their comments and was also required to be put up on the lead manager's website.

"The ICDR regulations do tweak the law in some respects, but a bulk of the changes reflect a formalisation of previously informal processes employed by SEBI," says Sandeep Parekh, former executive director-legal affairs, SEBI.

"The main purpose of the ICDR regulations is to convert the former guidelines into a form recognised by law. As SEBI Act makes violation of the Act, Rules, Regulations and directions subject to sanctions, it was not clear whether violation of a guideline could be subject to sanctions, particularly imposition of penalty. The conversion ensures that ICDRs stand on a much higher footing, as regulations are not only passed by SEBI, but are tabled in Parliament and are subject to explicit penalties and remedial actions," Mr Parekh added.

The ICDR regulations state that in case there are less than five listed group companies, the financial information is required to be given for all listed group companies, in addition for the largest unlisted group companies, so that the total number of listed and unlisted group companies does not exceed five.

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