



VINOD KOTHARI CONSULTANTS PVT. LTD.

Financial Consultants

Regd. Office: 1006-1009, Krishna Building, 224 A.J.C Bose Road
Kolkata-700017, India

Phone: +91 - 33 - 2281 7715 | 1276 | 3742

email: vinod@vinodkothari.com

Website: www.vinodkothari.com

www.india-financing.com

PAN No: AABCV0218P

Service Tax No: AABCV0218PST001

Corporate Identity Number: U74140WB1995PTC068742

27th November, 2014

To,
The Ministry of Finance
Department of Economic Affairs
Room No. 166-D, North Block,
New Delhi - 110 001

Sub: Representation on Legislative and other Changes for Bond Market in India.

Kind Attn: Mr. Anupam Mishra

Dear Sir,

We at Vinod Kothari Consultants Private Limited (VKCPL), a company focused on consulting and training services in the field of securitisation, asset-based financing and related areas, wish to humbly submit our representation suggesting legislative and other changes necessary to vitalize the Indian bond market.

Executive Summary

1. Highlight features of Indian bond market, not found elsewhere in the world:

- Issuer profile in India is dominated by financial sector while other non-financial entities hardly account for total issuances made in 2013-14.¹ Given the legislative framework there is no scope for non-financial corporates to issue bonds.
- Bonds in India are almost entirely secured bonds, whereas globally, unsecured bonds seem to be the norm.²

2. Permit unsecured Debentures to be issued to QIBs

- Unsecured debentures are treated as public deposits, which are allowed only to the extent of 25% of net worth of the issuer; in any case, too difficult and impractical for most issuers.
- Hence, debentures have to be necessarily secured. Most corporates, other than NBFCs, do not have assets to create charge in favour of bond/ debenture holders, as the assets are already charged in favour of banks.

¹ http://www.sebi.gov.in/cms/sebi_data/statistics/corporate_bonds/publicissuedata.html

² <http://www.bankofengland.co.uk/publications/Documents/quarterlybulletin/qb110403.pdf>



VINOD KOTHARI CONSULTANTS PVT. LTD.

Financial Consultants

Regd. Office: 1006-1009, Krishna Building, 224 A.J.C Bose Road
Kolkata-700017, India

Phone: +91 - 33 - 2281 7715 | 1276 | 3742

email: vinod@vinodkothari.com

Website: www.vinodkothari.com

www.india-financing.com

PAN No: AABCV0218P

Service Tax No: AABCV0218PST001

Corporate Identity Number: U74140WB1995PTC068742

- It is counter intuitive to expect a corporate to issue secured bonds; if the corporate had security to offer, it may be easier to access bank loans. It is when companies exhaust their security interests that they opt for bonds. Bonds are an incremental, additional source of funding, and not the first source of borrowing for most companies.
- There is no reason to restrict the bond markets to secured bonds, as long as the investor is a qualified institutional buyer (QIB) and/ or the bond issuance is rated. As QIBs can easily take a credit call on the issuer, the security offered is of no relevance. In any case, the security feature may be a question of pricing/ rating of the bond, and the regulation does not have to impose any fetters in this regard.
- The suggested change does NOT require a change of law – the same may be done by a minor amendment of the Companies (Acceptance of Deposits) Rules, 2014

3. Requirement of Debenture Redemption Reserve is completely misplaced

- DRR is simply an accounting reserve, not a fund.
- There is no other country in the world which insists on creation of a DRR.
- While DRR is inapplicable in case of certain private placements, it is applicable in case of public offers. This discourages companies from making public offers of bonds, and restricts the bond market to private placements only, which is not desirable.
- Not only is the DRR a drag on the distributable profits of the company, it also adds to the cost of issuance, since in the year of maturity, the issuer is required to create a funded DRR to the extent of 15% of the amount of debentures being redeemed.
- Therefore, the creation of DRR does not at all help in repayment of the debentures.
- DRR is completely unnecessary and should be done away with.
- No legislative change is required: exemption may be given by way of Rules u/s 71 of the Companies Act, 2013.

4. Companies Act, 2013 requiring charge on “Specific” Asset is creating difficulties

- Specific asset means ascertainable assets, which is in the nature of a fixed charge.
- As data shows, the issuers are predominantly (to the extent of about 98%)³ NBFCs

³ http://www.sebi.gov.in/cms/sebi_data/statistics/corporate_bonds/publicissuedata.html



VINOD KOTHARI CONSULTANTS PVT. LTD.

Financial Consultants

Regd. Office: 1006-1009, Krishna Building, 224 A.J.C Bose Road
Kolkata-700017, India

Phone: +91 - 33 - 2281 7715 | 1276 | 3742

email: vinod@vinodkothari.com

Website: www.vinodkothari.com

www.india-financing.com

PAN No: AABCV0218P

Service Tax No: AABCV0218PST001

Corporate Identity Number: U74140WB1995PTC068742

- The only assets on which NBFCs create security interest are receivables, which are in the nature of a current asset. The charge is, therefore, naturally, a floating charge.
- However, the insistence in The Companies (Share Capital and Debentures) Rules, 2014 on “specific” charge means there is a filing of a charge, and satisfaction of a charge, almost on a monthly basis. This condition is too difficult to comply, and is not serving any change
- Therefore the term specific restricts NBFCs from issuing bonds.
- No legislative amendment required; Rules may be amended by dropping the word “specific”.

5. Extend the benefit of SARFAESI Act to debenture trustees.

- The Act currently permits a trustee acting only on behalf of banks/ FIs to exercise the powers of the said Act and not where the bondholders are entities other than banks/ FIs.
- Necessary amendments may be introduced to include other debenture investors too.
- Under section 71 of the Companies Act, 2013 a debenture holder can enforce payment on a debenture only through CLB/ NCLT. In case of secured debentures, it should be possible to enforce security interest rather than invoke the jurisdiction of a quasi judicial authority.

6. Debt Recovery Tribunal (DRT) laws can also pass orders in the absence of security interest

- The Debt Recovery Tribunal (DRT) laws are equipped with a power to pass orders even where there is no security interest whereas SARFAESI Act has no such power.
- As per common practice in the market, banks use SARFAESI Act where there is security interest, and the DRT law where there is none, or insufficient security interest.
- Hence, DRT law may be activated even in case of unsecured bonds also.

7. Concerns arising from Companies Act, 2013(the ‘Act’) and allied rules

- Companies which have listed only debt securities, and not equity, are treated as “listed companies” under the Companies Act, and hence, are subjected to the whole discipline of the Act applicable to listed companies.



VINOD KOTHARI CONSULTANTS PVT. LTD.

Financial Consultants

Regd. Office: 1006-1009, Krishna Building, 224 A.J.C Bose Road
Kolkata-700017, India

Phone: +91 - 33 - 2281 7715 | 1276 | 3742

email: vinod@vinodkothari.com

Website: www.vinodkothari.com

www.india-financing.com

PAN No: AABCV0218P

Service Tax No: AABCV0218PST001

Corporate Identity Number: U74140WB1995PTC068742

- Typically, bond issues may be listed even by private companies.
- This is deterring companies from listing their bonds.
- Micro, Small and Medium Enterprises to get its debt securities listed the regulatory compliance burden may outweigh the benefits of price discovery, liquidity and transparency and the repercussion may be such companies may not be able to attract angel investors either
- Needs amendment of the definition of “listed company” under the Companies Act, 2013

A vibrant bond market for the corporate can ease financing constraints both in terms of cost of funds as well as ease of access to funds. On a macro-economic level development and growth in the capital markets leads to the development of the economy as well.

As VKCPL is dedicated to the cause of contributing to the development of the financial services sector and capital market instruments in particular, in the event of any further clarification needed, we would be happy to provide the same.

Thanking you,

Yours Faithfully,
For *Vinod Kothari Consultants Pvt. Ltd*

Sd/-

(Vinod Kothari)