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ADVOCATES, SOLICITORS & NOTARY

Multiple Regulators in the Bond Market

- The key concerns arise as a consequence of a number of regulators playing different roles in the bond market and there being no single window mechanisms to deal with the bond market
- Some of the regulators in the Bond market include
  - Securities and Exchange Board of India
  - Ministry of Corporate Affairs
  - Income Tax Authorities and the CBDT
  - Reserve Bank of India
- With each regulator having a different role to fulfil, streamlining the Bond market is very difficult

Reactive Policy Making

- While increasingly a consultative approach to policy making can be seen, there is still much scope for improvement
- For instance- last year's RBI circulars governing private placements mandating upfront creation of security, having minimum subscription amounts as well as spacing issuances by 6 months (later dropped in a subsequent clarification) caused much heartburn. Although a fallout of the Sahara case – this is a classic example of one regulator taking a stand without the full inputs from market makers.
- Having said that the positive of this is that the regulator was willing to reverse a change that was made once it was brought to the notice of the regulator in terms of the problems the same was causing.

Introduction of ‘residual maturity’-3 years and the withholding tax issue

- Recent RBI Circular-February 5, 2015- Prohibits FPI Investments in corporate bonds having a residual maturity of less than 3 years
- Hence no more ‘voluntary prepayment options’
- Affects investment strategies of FPIs and forces them to re-orient the same.
- One cannot question the rationale of the Reserve Bank of India to bring in long term investment instead of short term investment to protect against the foreign exchange risks.
- However this must also be weighed in mind in the absence of a uniform withholding tax policy for investors in corporate bonds.
- Under the Finance Act, 2013- WHT @ a concessional rate of 5% for interest payable on G-secs and rupee denominated bonds, provided for initial period of 2 years.
- Subsequently in 2015- The said concession was extended for a further period of 2 years- ending in June 2017.
- The conflict is clear – if you want long term bonds, you need withholding tax reductions also for long term as no investor can plan returns in a world of uncertainty

Applicability of Acceptance of Deposit Regulations

- For Companies to raise funds through private placements- Necessity of compliance with the Deposit Regulations needs to be relooked at, in the context of private placements.
- Everyone knows what really are deposits – bonds through private placements to educated and institutional investors do not constitute deposits. In other words it is time for the company regulator to state that so long as a bond is issued in terms of SEBI or RBI guidelines, it is exempt from deposits – why go down the traditional path of secured or unsecured – the regulators need to realise whose interest they are protecting

Clarity on the nature of 'subordinated debt' as applicable to NBFCs

- The definition of 'subordinated debt' as provided for in the NBFC Prudential Norms* is silent on the requirement of a min 5 year tenor.
- The NBFC Deposit Regulations on the other hand requires that only sub-debt having a maturity of not less than 60 months qualifies for the exemption of 'public deposit'.
- Rationale for having this unclear – since 90% of issues in the Indian market are through the private placement route with sophisticated investors who can take a call on risk.
- Further lack of clarity on insistence on not having restrictive clauses or any sort of early redemption option.

Regulator Cross Talk

- Several instances of the RBI and SEBI taking decisions independently and not in tandem even though there are aspects which both are concerned with.
- In the past, (Jan 2007)- Govt has clarified relevant areas of regulatory jurisdiction*. However there are still areas where it appears that channels of communication are not open
- For instance- Permissibility of FIIs/QFIs to invest in ‘to be listed’ debt securities came out in November, 2010. However as investments by FIIs/QFIs are regulated by RBI, the equivalent regulation permitting the same by RBI came out only in April, 2012

Some other Challenges

- Notification of debenture trustee as 'financial institutions' under the SARFAESI and the RDDBI Act.
- Presently, the Acts enable banks and financial institutions or debenture trustee acting for such banks/financial institutions to recover their dues. However DTs acting on behalf of common investors are not able to do so.
- Can be done by either amending the Acts or issuing a notification which in turn will give them the ability to recover debenture holders' dues.
- Another challenge is in terms of paper work – why would one need to file an information memorandum/ offer letter with the stock exchange as well as make one more information memorandum for an RoC filing under the Companies Act. Just adds to cost and paper work
- There are also issues around covered bonds which I understand will be dealt with in a later session today and therefore will not deal with the same.

Latest regulatory measures taken to improve bond market

- Permissibility of issuance of unsecured debentures by NBFCs – RBI circular of February 20, 2015
- Notification of debt listing norms for issuance of municipal bonds- SEBI July 2015
- RBI permission to banks- issuance of Long Term Bonds by Banks- towards infrastructure and low cost housing while providing certain regulatory incentives- RBI Circular of July 2014
- Permitting consolidation of past issues- Currently restricted to privately placed bonds- thereby ensuring illiquid and infrequently traded bonds can be re-issued 2015

Conclusion

- While we have dealt with a lot that can be done, it is not fair to say that nothing has been done.
- A lot has been done over the years by the various regulators to develop the bond markets. We must be thankful for the efforts over the years as the tasks today and the challenges today are not as heavy as one would anticipate.
- Our regulators are doing a lot and all that is needed is coordination between them and ensuring that there is no real overlap that happens in terms of roles. The regulators today are listening and are giving a lot of time and effort to streamline the market. As years go by, through trial and error our markets would develop further and have the necessary depth that we all would like it to have and it would be thanks to the regulators listening to everyone.

Thank You