# Note

## SEBI provides regulatory framework for non convertible preference shares


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# Article

Every business wants growth and growth needs fund. Business can arrange funds by various ways, major source of raising funds are by share capital or by debt. In return business needs to pay part of profit as divided and fixed rate of return as interest respectively. Preference shares are part of share capital but it is regarded as sort of debt as it carry fixed rate of dividend. Number of issuance and listing of non – convertible preference share have risen over Rs. 25000 crore in last three years1 and in absence of any regulatory ambit for the non convertible preference shares, a tight regulation was very much needed for providing the comprehensive framework.

## Need for Regulations

There are Securities and Exchange Board of India (Issue and Listing of Debt Securities) Regulations, 2008 which govern non-convertible debt securities and issue of equity and convertible securities by a listed company are governed by Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2009. For unlisted public companies, we have Unlisted Public Companies (Issue of Preferential Allotment of Securities) Rules, 2003 in place which regulate issue of equity and convertible securities issued on preferential basis. However, there were no such regulation which governed the issue and listing of non-convertible redeemable preference shares. .As a result of huge fund raising through non convertible preference shares, SEBI has decided to govern the issue of such shares also. Accordingly, it has on June 12, 2013, has issued SEBI (Issue and Listing of Non-Convertible Redeemable Preference Shares) Regulations, 2013, ("Regulations") which has come into effect with immediate effect. Prior to issue of final Regulations, SEBI in continuation of its press note 27/2013 [2]had notified the regulation.

[1] http://businesstoday.intoday.in/story/sebi-sets-new-norms-for-listing-of-preference-shares/1/193152.html
[2] http://www.sebi.gov.in/sebiweb/home/detail/25447/yes/PR-SEBI-Board-Meeting

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## Applicability of Regulations

This regulation shall be applicable to the followings:

a. Public issue of non-convertible redeemable preference share
b. Listing of such share on recognized stock exchange issued by a public company through public issue or private placement.
c. Issue and listing of Perpetual Non-Cumulative Preference Shares and Perpetual Debt Instrument, issued by banks on private placement basis in compliance with Guidelines issued by Reserve Bank of India.

## Important Definition for understanding the regulation

Non-convertible redeemable preference share" means a preference share which is redeemable in accordance with the provisions of the Companies Act, 1956 and does not include a preference share which is convertible into or exchangeable with equity shares of the issuer at a later date, with or without the option of the holder;

Perpetual non-cumulative preference share" means a perpetual noncumulative preference share issued by a bank in accordance with the guidelines framed by the Reserve Bank of India;

Private placement" means an offer or invitation to subscribe to the non convertible redeemable preference shares in terms of sub-section (3) of section 67 of the Companies Act, 1956;

Perpetual Securities: Perpetual security, usually in the form of a corporate bond or other debt instrument, is issued by a company without any obligation to redeem it from the investors. Such an instrument only provides a steady income flow to the investor. In that sense, it is akin to equity, and ranks fairly low in priorities. The issuer may, however, retain a call option whereby it might wish to redeem the security at some point in time. Although a fairly old instrument, I have begun to notice its use more often in the last couple of years, especially in the Asian markets.

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## Specific requirements under Regulations, 2013

- Application of listing must be made to one or more recognized stock exchange which has nationwide trading terminal and issuer must recognize one of them is designated stock exchange
- Issuer must obtain minimum rating of "AA-'' or equivalent from SEBI registered credit rating agency.
- Public issue must be made in accordance with Depository Act,1996 and regulation made there under.
- Minimum tenure of non-convertible redeemable preference share should be 3 years.
- Creation of Capital redemption reserve accordance with Companies Act,1956 is mandatory.
- The lead merchant banker shall, prior to filing of the offer document with the Registrar of Companies, furnish to the Board a due diligence certificate as per Schedule II of these regulations.
- Minimum application size for each investor should be 10 lakh rupees.
- Each rating obtain by issuer shall be reviewed by registered credit rating agency annually.

## Conclusion

The introduction of this regulation provide larger elasticity to companies to raise capital, it is essential to pay concentration to the risks involved, measures must be taken to protect the interests of the investors. This regulation may impose adverse effect on foreign investment as the regulation required compliance with ECB guidelines.