

## ERGO

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### DELISTING DYNAMICS: UNPACKING REGULATORY COMPLEXITY

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#### *Introduction*

The Securities and Exchange Board of India (Delisting of Equity Shares) Regulations, 2021 (Delisting Regulations) sets out a detailed mechanism for promoters to delist listed companies while ensuring that all public shareholders are provided a fair and equitable exit. Under the erstwhile regime, the exit price was determined through a reverse book building (RBB) process based on the prices at which bids were placed by public shareholders as they deemed fit. However, an announcement of a delisting offer often results in increased market price volatility, accumulation of shareholding by some shareholders and inflated/ exorbitant bids in the RBB process.

As a result of such speculative bidding activities and inflated exit price expectations, several delisting offers have failed over the years as promoters have found the final exit price to be commercially unviable. In order to address concerns such as these, the Securities and Exchange Board of India (SEBI) has recently announced numerous amendments to the Delisting Regulations effectively overhauling the entire regime. This article sheds light on the key changes introduced by the recent amendments and their likely impact on the overall delisting process.

#### *New fixed price delisting mechanism*

The most significant amendment is the introduction of a fixed price mechanism as an alternative to the existing RBB process. Under this mechanism, if a target's shares are frequently traded, its promoters may offer a fixed delisting price to the public shareholders. The fixed price must be at a premium of at least 15% over the floor price (*please refer to the section below for further details regarding floor price*). Each public shareholder may either choose to accept the fixed price that is offered and tender their shares or reject the offer. The delisting would succeed if the shares tendered by the public shareholders push the promoters' shareholding to 90% or more.

**Comment:** *Under this mechanism, public shareholders are left with a binary 'yes' or 'no' option thereby negating the risks of the RBB mechanism wherein public shareholders are free to place bids at any price as they deem fit. This steers the delisting offer clear of any price uncertainty and enables the promoter to make funding arrangements upfront. However, the effectiveness of this mechanism remains to be seen as public shareholders may just choose not to tender shares if they are not satisfied with the premium offered over the floor price, thereby resulting in failure of the delisting offer. As counter-offers are not permissible under the fixed price mechanism, promoters who want to attempt delisting again will have to re-commence the process from scratch.*

#### *Determination of floor price*

The floor price plays a significant role in the fixed price mechanism (as mentioned above) as well as for the RBB process (as the floor price is the minimum price at which bids are placed). Prior to the amendment, the highest of *inter alia* the following parameters was the floor price:

1. Volume weighted average price paid/ payable for any acquisitions of shares by the promoters during the 52 weeks preceding the reference date.
2. Highest price paid/ payable for any acquisitions of shares by the promoters during the 26 weeks preceding the reference date.
3. If the shares are frequently traded, volume-weighted average market price (VWAMP) during the 60 trading days preceding reference date.
4. If the shares are infrequently traded, price determined taking into account valuation parameters such as book value, comparable trading multiples, and such other parameters as are customary for valuation of shares of such companies.

The amendment introduces "adjusted book value" as an additional parameter to be considered for determining floor price. This is applicable irrespective of whether the target's shares are frequently traded or not. A detailed formula has been prescribed by SEBI requiring the consideration of inter alia the following:

1. The book value of assets of the target.
2. Fair market value of unlisted and infrequently traded listed shares held by the target as determined through valuation.
3. Fair market value of listed shares held by the target based on the transaction value of such shares on the stock exchanges.
4. Value of immovable property held by the target based on the value adopted/ assessed by any Government authority for the purpose of payment of stamp duty.

Liabilities as shown in the balance sheet (with some exceptions) are to be deducted.

**Comment:** *The erstwhile mechanism for determining floor price was derived from the regime applicable to open offers (where companies remained listed post offer), which may not be appropriate for delisting offers. For instance, in cases where shares were frequently traded, market prices of the target played a major role in determining floor price and the actual value of the assets of the target were disregarded (especially where market prices were significantly discounted). The introduction of adjusted book value as an additional parameter, which mirror certain valuation techniques under income tax provisions, is likely to enhance the accuracy of the floor price in the context of delisting offers as it would now reflect the value of the assets and liabilities of the target. This may reduce public shareholders' expected premium, thereby increasing delisting process certainty.*

### Reference date

Under the erstwhile regime, the reference date for determining the floor price was the date on which the stock exchanges were to be intimated by the target regarding the proposed board meeting to consider and approve the delisting proposal. By such date, the market price would have been affected by the news of the delisting as the promoters would have already issued an initial public announcement regarding the delisting offer.

SEBI has now amended the reference date to be the date of the initial public announcement itself. Where the initial public announcement is made after trading hours, the reference date will be the day following the initial public announcement.

**Comment:** *This ensures that unaffected market prices are considered for determining floor price, effectively negating the effects of any market price volatility once the news of the delisting is in the public domain.*

### Counter-offer mechanism

In a delisting offer undertaken through the RBB process, promoters can make a counter-offer if the price determined through the RBB process is not acceptable. Earlier, such counter-offer could have been made only if the total shares tendered in the RBB took the shareholding of the promoters to at least 90%. SEBI has reduced this threshold to 75% provided at least 50% public shareholding has been tendered.

**Comment:** By reducing the threshold, delisting offers that were set to fail due to low tendering (since the 90% threshold was not met) may be salvaged by the promoters through a counter-offer. They would have an opportunity to re-evaluate the delisting price and offer a price that may be more likely to see higher tendering.

Further, the minimum counter-offer price was the book value of the target. Pursuant to the amendment, the minimum counter-offer must now be the higher of: (i) the indicative price offered by the promoters while making the delisting offer, if any; and (ii) the volume weighted average price of the shares tendered under the RBB process. SEBI has also clarified that the prices of only those shares tendered that take the promoters' shareholding to 90% are required to be considered for arriving at the volume weighted average price.

**Comment:** The focus on prices of bids in the RBB process will help in ensuring that counter-offers are better aligned with the expectations of public shareholders.

### **New regime for delisting investment holding companies**

The amendments have introduced a new mechanism to delist investment holding companies (IHCs), i.e., entities that have at least 75% of their fair value (net of liabilities) comprising direct investments in equity shares of other listed companies. Promoters of IHCs that have been listed for at least 3 years now have an option to delist such targets through the following mechanism:

1. Listed shares held by the target (net of pro-rata liabilities) are to be distributed to the public shareholders of the target in proportion to their shareholding.
2. Cash payments must be made by the target, in exchange for the unlisted shares and other assets of the target, to the public shareholders in proportion to their shareholding.
3. Thereafter, the shares held by public shareholders in the target are extinguished pursuant to a scheme of selective reduction of capital and the target is delisted.

Certain additional conditions have been introduced, including the requirement to adhere to the provisions applicable to schemes of arrangement under the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 and the circulars thereunder.

**Comment:** The new mechanism provides a novel way to delist IHCs without placing large funding obligations on the promoters. As dilution of holding in listed investee companies held by the target would be a concern, it is likely that this mechanism would be preferable only in cases where the promoters' shareholding in the target and target's shareholding in listed investee companies are high.

### **Conclusion**

The amendments to the Delisting Regulations are a clear indication of the regulator being proactive in addressing several of the concerns faced while attempting a delisting. Promoters of listed companies now have a variety of options to choose from based on what would best suit their circumstances. Nevertheless, the focus on ensuring that public shareholders receive a fair and equitable exit remains. The success of these new mechanisms and the amendments to the RBB mechanism will certainly be tested in the years to come.

- Arindam Ghosh (Partner), Abhishek Dadoo (Partner), Shashank Patil (Counsel), Anvita Mishra (Principal Associate), Gaurang Mansinghka (Associate) and Shubhra Wadhawan (Associate).

For any queries please contact: [editors@khaitanco.com](mailto:editors@khaitanco.com)