



Unlocking Value Of Unlisted Players Via IPOs Enroute India's Booming Long Term Economy

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Indirect conducive contributors

As India steadily moves towards the upcoming general elections in April-May 2024 anticipating an optimistic result, Indian Capital Markets is one sure shot domain which is likely to yield benefits across the entire spectrum.

Global brands are continuously queuing up to set up Indian operations forecasting the benefits of our developing nation. Similarly on the investment receiving side, various state focused roadshows were recently set up and also broadcasted during the World Economic Forum's Annual Conference 2024 in Davos.

Certain marquee investors have also publically echoed their intentions towards India especially given the reasonable valuations currently poised for Indian players vis-a-vis their peers offshore. This is also a testament of India being the sought after growing nation even amongst the BRICS group.

Infact, on the lines of the Ease of Doing Business in India programme, the demographics of the applicants in the recent Initial Public Offerings ("IPOs") is also highlighting that a younger generation first time investor base on the click of few buttons on electronic platforms are opening demat accounts and bidding for the IPOs via the application supported by blocked amount mechanism developed by the Securities and Exchange Board of India ("SEBI").

Moreover, the Government of India has also been encouraging, growth and development of Indian Capital Markets via distinct channels such as the International Financial Services Centre ("IFSC") pursuant to which, a direct listing of Indian public companies on IFSC exchanges has just been made achievable. Similarly, the SEBI continuously evaluates the extant norms in order to make it business friendly within the corners of law



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basis live developments including by issuing public consultation papers for proposed regulatory changes and is recently exploring usage of artificial intelligence for reviewing offer documents as well.

IPO Check Points

Before kick starting, an issuer needs to process certain hygiene checks by ensuring able and (preferably) dedicated core IPO team members including a Chief Financial Officer and a Company Secretary.

This journey involves a variety of decisions to be taken, individually and collectively, by the issuer, promoters, investors, merchant bankers and counsels, amongst other parties. Certain of these key to-do items have been listed below:

Eligibility: While conversion into a public limited company (under the Companies Act, 2013, as amended) is a pre-requisite, the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018, as amended (the "SEBI ICDR Regulations") bans the following from accessing Capital Markets: a) any issuer, promoters, promoter group, selling shareholders debarred by SEBI, b) any promoters or directors associated with any other SEBI debarred entity, c) any issuer, promoters and directors identified as wilful defaulters/fraudulent borrowers or d) any promoters and directors identified as fugitive economic offenders.

Moreover, all outstanding convertibles / stock options (except options of a SEBI compliant scheme/plan), are to be diluted by the red herring prospectus ("RHP") filing stage. Further, the bourses do not allow any IPO listing wherein any insolvency/bankruptcy, winding up or industrial and financial reconstruction proceedings are ongoing with respect to the issuer.

Furthermore, pursuant to Regulation 6 of the SEBI ICDR Regulations, the regulator also mandates certain financial metrics related to net tangible assets, average operating profit, net worth and revenue, for determining the IPO subscription allocation matrix to be followed for qualified institutional buyers, retail and non-institutional investors.

Promoter identification: Persons who have been named as such in an offer document or annual return or has control over the issuer's affairs or on whose advice, directions or instructions, the issuer's board acts, typically fall under the bucket of 'promoter'. Except if the person is acting in a professional capacity or if the shareholding is 20% or more merely as an investor. The objective is to ensure that persons actually having a skin-in-the-game are identified as promoters and consequently, corrective steps may also be required for parties loosely identified as promoters in historical annual returns. The promoter group set of parties will also have to be determined pursuant to a formula as detailed in the SEBI ICDR Regulations.

Offer Structure: Stemming from the Securities Contracts (Regulation) Rules, 1957, as amended, to comply with the timely minimum public shareholding ("MPS") requirements for a to-be listed company, following

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structures will have to be tested in order to determine the IPO dilution required:

Post-IPO Share Cap	Minimum IPO size	Time period for MPS*
≤ INR 1,600 crs	25%*	NA
INR 1,600 crs up to INR 4,000 crore	Share value of at least INR 400 crore	Within 3 years post IPO
≥ INR 4,000 crs up to INR 1 lac crore	10%*	Within 3 years post IPO
≥ INR 1 lac crore	Share value of at least INR 5,000 crore and ≥ 5%*	10% & 25% within 2 & 5 years, respectively, post IPO

*Post-IPO share cap
*Minimum 25% public holding

Moreover, for an offer for sale component in the IPO, the issuer will have to send an invitation to all its shareholders to sell all/any of their shares via the IPO and primarily indicating, amongst other criteria, that the sellers should have a minimum holding period of 1 year pre-draft red herring prospectus ("DRHP") filing (including any convertibles which must be converted before RHP).

The selling shareholders also have the have right to withdraw its offered shares at an appropriate time (before RHP filing), subject to contractual and commercial understanding with the issuer and the merchant bankers. However, a change in the offer for sale size (as disclosed in the DRHP) by more than 50%, will result in re-filing of the DRHP with SEBI for another approval.

Moreover, in case of an IPO under Regulation 6 (2) of the SEBI ICDR Regulations, the OFS size may have to be tailored basis shareholding amongst the sellers.

Private Equity investors' first order of business: Amendment of the existing shareholders' agreement and the articles of association of the issuer to be factored-in for wiping of all the special rights of the pre-IPO investors with effect from an appropriate time of filing the RHP with the regulators. Any upside sharing arrangement between certain shareholders of an unlisted company must be consummated before listing.

Business & Industry story: Merchant banker's analyst will brain-storm with the promoters and senior management to deep dive into the issuer's business model and back-off-the-envelope valuation. Similarly, the banker's marketing teams will also loop in an appropriate sector industry expert in order to chip-in to the overall IPO pitch material (including the offer documents).

Financials: Existing standalone & consolidated audited financials prepared under the Indian Generally Accepted Accounting Principles (if any) will have to transformed to special purpose financial statements under the Indian Accounting Standards (except in case of banking & finance players)

for last 3 years and stub period, which shall then be valid for 135 days until filing of the DRHP/RHP, depending upon the kind of IPO under foreign securities laws. Such financials are required to be restated by a peer reviewed and independent, statutory auditor or chartered accountant, in accordance with the SEBI ICDR Regulations. In case of any proposed/completed acquisition/divestment by the issuer/subsidiary, applicable proforma financials for latest fiscal & stub period (if any) will have to be processed, subject to triggering certain criteria under SEBI ICDR Regulations. The proforma financials may also be voluntarily disclosed for any immaterial acquisition/divestment (proposed or completed) so as to appropriately reflect the relevant business verticals spread across the issuer (on a consolidated basis).

Other key financial info (i.e. net asset value, earnings per share (basic/diluted), return on net worth & earnings before interest, taxes, depreciation and amortization) will also be essential metrics for offer documents and related marketing material.

End-use of IPO money: Determine the IPO objects basis the projected needs for next 2-3 years and align it with the past & future growth story proposed to be reflected in the business sections of the DRHP and other roadshow material. More importantly, avoid a delta in objects size by more than 20% at the launch stage from what was disclosed in the DRHP failing which it has to be refilled for SEBI approval. Routine objects for consideration are: a) debt retirement, b) capex, c) working capital, d) investment in subsidiary and e) capital augmentation (for banking & finance sector). General corporate purposes as an object can be capped

upto 25% of the gross proceeds of the fresh issue component in the IPO and it is advised to avoid any bridge financing arrangements.

Corporate Governance: Setting up an adequate combination of executive and independent directors as well as the vital committees is of paramount importance for all stakeholders. It is imperative that issuers prioritize best corporate governance practices from the day of IPO kick-off in order to gain trust and confidence of prospective IPO investors and shareholders of the newly listed company as well.

Due Diligence: Granular exercise will have to be conducted to identify bottle necks and long lead items with respect to the issuer (on a consolidated basis) especially involving the capital structure, corporate and secretarial compliances, litigation, approvals, third party consents and business information.

Minimum Promoters Contribution & Lock-In: Minimum 20% of the post-IPO share capital to be locked-in by the promoter(s) for 18 months provided such shares have been acquired for cash or as bonus on eligible shares, and must be free from any pledge/encumbrance. Shortfall if any, in the above contribution, may be achieved via

certain other eligible holders subject to certain conditions. Moreover, SEBI, via its consultation paper dated January 11, 2024 has proposed to enable non-individual non-promoter shareholders holding between 5 to 10% of the post-IPO share capital to assist in bridging this gap for achieving the 20% mark. Residual pre-IPO holding of all existing shareholders* (including all promoter shareholding, in excess of the minimum promoter contribution - 20% of share capital for 18 months) must be locked in for 6 months from date of allotment in the IPO.

**Excluding ESOP shareholders and for certain other shareholders it has to be locked-in for 6 months from date of share purchase*

Appointment of intermediaries: Besides, merchant bankers and counsels, the issuer will also have to involve, peer reviewed and independent, statutory auditor, chartered accountant, chartered engineer, as applicable, escrow bankers, syndicate members, registrar and advertising agency, amongst others.

Life as a Listed Company

Inherently the obligations of a listed player are manifold vis-a-vis an unlisted entity. Consequently, it is imperative for issuers to upgrade their systems including for human capital as their responsibility is now extended to a broader shareholder base. Accordingly, there is a wide gamut of compliances to be adhered to as a listed company, drafted by SEBI, bourses and applicable sector regulator such as the Reserve Bank of India.

As an example, one of the critical nascent steps to be exercised by a newly listed Company, is regarding its financial statements. Basis the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations 2015, as amended, it has been mandated that in order to bridge the gap in the publicly available financials i.e. via the final offer document aka the prospectus and immediately post listing, the audited or unaudited financials for the relevant quarter or fiscal are to be submitted within 21 days of listing or 45/60 days (in case of quarter/fiscal period, as applicable), whichever is later. In similar vein, there are various other regulations, circulars, FAQs, informal guidances, consultation papers (for tracking future norms) issued by the above mentioned draftsmen, which will have to be closely monitored and adhered to, from time to time.

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Siddhartha specializes in public and private Capital Market transactions. He has advised various issuers, underwriters and selling shareholders on equity offerings such as initial public offerings, rights issues, qualified institutions placements, institutional placement programmes & infrastructure investment trusts (InvITs), and debt offerings such as non-convertible debenture issuances. His scope of work in these transactions included conducting due diligence, drafting & reviewing offer documents, participating in drafting sessions, negotiating transaction agreements and other offering related documents and public filings.



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