UPDATES

TRILEGAL

SEBI's revised framework for issuance of observations on draft offer documents in public offerings

18 March 2020

This update covers:

1 Introduction

SEBI has revised timelines for issuance of observations on a draft offer document to provide more clarity for cases where adverse proceedings are probable or ongoing against the issuer or its directors, promoters or group companies.

When an offer document is filed by an issuer with the Securities and Exchange Board of India (**SEBI**), SEBI on its review can either prohibit the company from issuing the prospectus or offer document or provide observations specifying conditions subject to which these can be issued.

On 8 December 2006, SEBI issued the SEBI (Issuing Observations on Draft Offer Documents Pending Regulatory Actions) Order, 2006 (**2006 Order**) to formalise the issuance of observations on draft offer documents filed for a public offering (**Observations**), where an investigation, enquiry, adjudication, prosecution or other regulatory action is pending against the issuer or its promoters/directors/group companies (collectively, the **Parties**). On 5 February 2020, the 2006 Order has been replaced by the SEBI (Issuing Observations on Draft Offer Documents Pending Regulatory Actions) Order, 2020 (**General Order**) to streamline and bring certainty to timelines for the issue of Observations by SEBI.

While determining the permissibility of a public offering, SEBI takes into consideration pending adjudicatory, regulatory and other proceedings against the Parties and therefore timelines for the issuance of Observations are critical. Although the 2006 Order clarified the approach and timelines for keeping Observations in abeyance (if a probable cause of violation was found or show cause notice issued), it did not adequately address timelines to be followed for keeping Observations in abeyance when proceedings against Parties were not concluded within given timelines for reasons beyond SEBI's control or owing to the conduct of the Parties themselves. Further, there was no provision to address cases where (i) proceedings for recovery against any of the Parties was initiated by SEBI; (ii) an order for disgorgement or monetary penalty was passed against any of the Parties and was not complied with; (iii) any direction issued by SEBI was not complied with by any of the Parties; or (iv) the issuer was restrained by a court from making a public issue or filing offer document.

The General Order therefore addresses some of these gaps.

2 Key Changes

2.1 Reduction in timeline for keeping Observations on draft offer documents in abeyance to 30 days (earlier 45 days)

Where there is a probable cause for investigation/enquiry or where an investigation or enquiry is ongoing, the timeline for keeping Observations in abeyance has been reduced to 30 days (earlier 45 days) from the later of, (i) the date of such probable cause of violation being found; or (ii) the date of filing of the draft offer document.

Further, the General Order provides that if SEBI cannot conclude proceedings within this period for reasons beyond its control or owing to the conduct of entities other than the Parties, Observations should be kept in abeyance for a further 30 days. However, if the delay in concluding proceedings is due to the conduct of any of the Parties, Observations should be kept in abeyance until the conclusion of the investigation, enquiry or examination.

2.2 Timeline where show-cause notice is issued and conclusion of proceeding is delayed

Under the 2006 Order, if a show-cause notice was issued to Parties, Observations were to be kept in abeyance for 90 days from the filing of the draft offer document. In the absence of an interim or final order within this period, the Observations were issued, subject to relevant disclosures in the offer document about the show cause notice and the possible adverse impact of an order.

The General Order retains the timeline provided under the 2006 Order, but clarifies that if SEBI cannot conclude proceedings in 90 days for reasons beyond its control or owing to the conduct of entities other than the Parties, Observations should be kept in abeyance for a further period of 45 days. Then again, where the delay is due to the conduct of the Parties, the General Order provides that the Observations should be kept in abeyance until the conclusion of the proceedings.

2.3 Observations in cases of recovery proceedings, imposition of monetary penalty or non-compliance with SEBI directions

The General Order introduces timelines for keeping Observations in abeyance where:

a. proceedings for recovery against any of the Parties is initiated by SEBI;

b. an order for disgorgement or monetary penalty is passed against any of the Parties and is not complied with; or

c. any direction issued by SEBI is not complied by any of the Parties.

In such cases, Observations are to be kept in abeyance till the proceedings are concluded or until the directions are complied with.

2.4 Disclosure of adverse impact in offer documents

The General Order also provides that if a show-cause notice has been issued by any authority against the Parties in an adjudication proceeding, SEBI may issue Observations and direct the issuer to make necessary disclosures in the offer documents about such proceeding, including any probable adverse impact of such an order on the Parties.

2.5 Observations with riders attached

In those cases where an issuer has been restrained by a court or tribunal from making an issue of securities or from issuing offer documents to the public, the General Order makes provision for the issue of Observations with a qualification that any proposed issuance will be subject to the orders of the appropriate authorities.

3 Conclusion

Where earlier there was uncertainty on the timelines for issue of Observations and the approach to be adopted during pendency of proceedings, the General Order has provided much needed clarity by providing that the pendency of proceedings does not automatically create a bar to a public offering.

However, to address the situation where Parties would intentionally delay proceedings hoping to receive Observations in the interim, the General Order enables SEBI to identify such cases and keep Observations in abeyance until the conclusion of those proceedings. On the other hand, there is no clear explanation for what constitutes 'conduct of the Parties', and therefore there is likely to be a degree of discretionary determination by SEBI in such cases.

The General Order is a significant improvement over the 2006 Order and should bring more clarity and certainty in the process and timelines for the issue of Observations.