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Unlocking Global Opportunities: A Comprehensive Analysis of The MCA's Amendment Allowing Indian Companies to Directly List on Foreign Stock Exchanges

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ABSTRACT

The recent notification of the Ministry of Corporate Affairs with regard to the direct listing of Indian equity shares in the foreign stock exchange is a very crucial step. Earlier the listing in foreign exchange was done through the use of ADRs/ GDRs. This was a lengthy process as it required an underwriter and usually, this took a long time. Furthermore, this route has witnessed many corruption such as round tipping of funds and money laundering. Later on, the expert committee of SEBI also published the report for direct listing of equity shares in the foreign stock exchange. The committee made various recommendations regarding the same. The Ministry of Corporate Affairs then came up with the new amendment allowing the Indian Companies to directly list its share in the foreign stock exchange.

There are multiple sections to this article. First, the article provides a brief synopsis of the circumstances surrounding the amendment's ratification. Second, it discusses the traditional ADR/GDR route, which required Indian Companies to convert their securities into depository receipts in order to obtain funding from foreign stock exchanges. Thirdly, it addresses the amendment made to the MCA that permits the direct listing of equity shares on foreign stock exchanges. Finally, it analyzes the noteworthy example of companies that directly listed their shares and provides insight into past events that have operated as a barrier in the path of Indian companies from listing on foreign stock exchanges.

However, there is a lack of regulatory framework which creates confusion. For instance, the Foreign Exchange Management Act, 1999, and Companies (Prospectus and Allotment of Securities) Rules 2014 have not been amended. Hence, in the absence of any regulatory frameworks, the amendment only acts as a licence to direct listing without any appropriate procedure.

Keywords: *Direct listing, Amendment, Foreign Stock exchange, Expert committee.*

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I. INTRODUCTION

The recent amendment of the Ministry of Corporate Affairs brought relief to the companies incorporated in India. The amendment was made in the Companies Act according to which the domestic companies can directly list their equity share in International Financial Service Centre (IFSC), Ahmadabad. The traditional method of gaining money from foreign capital market by way of converting the shares into depository receipts (ADR or GDR) which are now done away with.

In the backdrop there had been many recommendations regarding the direct listing of shares. On 4th December 2018, the expert committee of SEBI published a report recommending the direct listing of equity shares of companies incorporated in India on foreign stock exchange.³ The committee recommended the amendment as it would bring great benefits to the Indian companies willing to list their equity shares in the foreign capital markets. It would help the Indian companies to raise capital from the foreign stock exchange.⁴

The procedure of the listing of Indian companies into foreign stock exchange through ADR/GDR has been very lengthy and time consuming. Due to this, the companies have always refrained from listing their shares on the foreign stock exchange. The recent data reveals that there have been only 109 companies from 2008-2018 that have invested in the foreign country through the ADR/GDR method.⁵ This is in some way also limited the companies' ability to raise capital. Hence, the new amendment has tried to solve these issues and allow Indian companies to directly list on foreign stock exchanges without converting the shares into depository receipts. It has thereby eased the process of raising capital.

II. THE CONVENTIONAL ADR/GDR PATH AND THE CHALLENGES IT POSES

For Indian companies to raise capital from the foreign stock exchange it was mandatory for the Indian companies to convert their shares into depository receipts. The conversion of the shares to depository receipts involved strict regulatory requirements and entry norms. When it came

³ Report of the Expert Committee for Listing of Equity Shares of Companies Incorporated in India on Foreign Stock Exchanges and of Companies Incorporated Outside India on Indian Stock Exchanges, (Dec. 4, 2018), https://www.sebi.gov.in/reports/reports/dec-2018/report-of-the-expert-committee-for-listing-of-equity-shares-of-companies-incorporated-in-india-on-foreign-stock-exchanges-and-of-companies-incorporated-outside-india-on-indian-stock-exchange_41219.html.

⁴ Press Release, Securities and Exchange Board of India, Expert Committee for Listing of Equity Share Capital of Companies Incorporated in India on Foreign Exchanges and Vice Versa (Dec. 4, 2019), https://www.sebi.gov.in/reports/reports/dec-2018/report-of-the-expert-committee-for-listing-of-equity-shares-of-companies-incorporated-in-india-on-foreign-stock-exchanges-and-of-companies-incorporated-outside-india-on-indian-stock-exchange_4121.

⁵ Hitesh Vyas, *Direct Listing on Foreign Exchange: What Does it Mean for Indian Companies?*, THE INDIAN EXPRESS, November 3, 2023.

to the issue of capital in American stock exchange American Depository receipt (ADR) is used while in any other nation global depository receipt (GDR) is used. In other words, it's essentially a kind of negotiable instrument used to transact foreign assets. By simply transferring the ADR, the holder is able to transfer title to the underlying foreign stock shares. A U.S. depository represents a foreign private issuer whose equity shares are issued as receipts.⁶

Before the current amendment, the Indian companies followed this route (of DRs) and in order to convert their securities into depository receipts the companies had to follow the provisions of the Companies Act, 2013, the Foreign Exchange Management Act, 1999, Prevention of Money Laundering Act, 2002 and rules and regulations thereunder. In 2019, SEBI issued a circular that dealt with the issue of depository receipts and the procedure to be followed.⁷ It drew attention to section 41 of the Companies Act, 2013 and the Depository Receipts Scheme, 2014. The circular mainly lays down specific compliance and procedures for the listed Indian companies intending to issue or transfer Permissible Securities for depository receipts. It further lays down that the companies must follow (i) the guidelines laid down by SEBI, (ii) no debarment from the capital market and, (iii) not involved under any wilful default or have any association with any fugitive economic offender.

SEBI had close scrutiny over the GDR route whereby it found various allegations of round-tripping. It entails a party transferring money or assets under false pretenses of a commercial transaction with the intention of buying them back later on while completely circumventing all financial rules. Further SEBI also expressed its concern about the difficulty to track such cases and hence is an essential cause of money laundering and market manipulations.⁸ In 2010 SEBI also banned Sanraa Media for manipulating the share prices using GDR.⁹ Further, in 2017 SEBI barred 19 domestic companies for manipulation in GDRs and on the other hand K Sera Sera Ltd and Asahi Infrastructure and Projects Ltd. were banned for 10 years over the same issue. Hence round-tripping of funds has been a major cause of laundering black money.^{10 11}

The issues arising due to the traditional routes were constantly increasing and hence to deal with it the expert committee of SEBI published a report on 4th December, 2018 suggesting direct listing of equity shares.¹²

⁶ Lander, Guy P., *American Depository Receipts*, 29 THE INTERNATIONAL LAWYER, 897–915 (2018).

⁷ Security Exchange Board of India, SEBI/HO/MRD/DOP1/CIR/P/2019/106, (Oct. 10, 2019).

⁸ Bhumesh, *supra* note 1.

⁹ Press Trust of India, *GDR issue: Sebi bars Sanraa Media*, THE MINT, April 3, 2017.

¹⁰ Bhumesh, *supra* note 1.

¹¹ KII Limited v. Securities and Exchange Board of India, 2018 SCC OnLine SAT 122 (India).

¹² *Id.*

III. THE MCA'S AMENDMENT

The Ministry of Corporate Affairs (MCA) of India is a government ministry for regulating corporate affairs and ensuring compliance with various company laws. The objective of this Ministry is to reinforce corporate governance, strengthen the ethical business culture in India, and to ensure the freedom of trade to be carried on by the participants of India. Acting upon the recommendations of the expert committee¹³ and request of various corporate entities the Ministry of Corporate Affairs took cognizance of the matter and amended the Companies Act per se allowing the Indian companies to directly list in foreign stock exchange. The object of the Ministry of Corporate Affairs is to strengthen corporate governance and strengthen the ethical business culture in India. It also ensures the freedom of trade to be carried on by the participants of India.

Through this, amendment govt. is allowing direct listing on foreign exchange and the following are the amendments that have been brought in this regard in the Companies Act, 2013:

Section 2(52) defines Listed companies as “*a company which has any of its equity shares listed on any recognized stock exchange*”.¹⁴ The amendment has included a proviso:

*"Provided that such class of companies, which have listed or intend to list such class of securities, as may be prescribed in consultation with the equity shares and Exchange Board, shall not be considered as listed companies."*¹⁵

This proviso has been inserted to exempt companies that list their stocks on foreign stock exchange from following certain Indian regulations. Specifically, It releases them from following the conditions provided in the Indian Listing Regulations (LODR). Alternatively, these companies can comply with the disclosure laws of the foreign nation in which they will be listed. In simpler terms, a company that offers its equity shares abroad is free to abide by the regulations of the foreign stock exchange it is listed on, rather than to follow specific rules in India.

Further, on 30th October, 2023, the Ministry of Corporate (MCA) Affairs issued a notification regarding the implementation of section 5 of the Companies (Amendment) Act, 2020. It has basically incorporated the sub-sections (3) and (4) into section 23 of the principal Act.

(A) The Amendment to Section 23

¹³ *Id.*

¹⁴ Companies Act, Act, 2013, § 2(52), No. 29, Acts of Parliament, 2013 (India).

¹⁵ *Id.*

This section outlines the procedures through which both private and public companies can issue equity shares and raise funds from the Indian capital market. The specified methods are explained in Sub-sections (1) and (2), which include Public Offer, Private Placement, Right Issue, and Bonus Issue. The Companies (Amendment) Act of 2020, on the other hand, has made it possible to issue equity shares through a new route that entails listing on a foreign stock exchange. The newly incorporated sections are:

“(3) Such class of public companies may issue such class of equity shares for the purposes of listing on permitted stock exchanges in permissible foreign jurisdictions or such other jurisdictions, as may be prescribed.

(4) The Central Government may, by notification, exempt any class or classes of public companies referred to in sub-section (3) from any of the provisions of this Chapter, Chapter IV, section 89, section 90 or section 127 and a copy of every such notification shall, as soon as may be after it is issued, be laid before both Houses of Parliament.”¹⁶

This legal provision, mentioned in Sub-Section (3) permits only a particular class of Public companies as may be prescribed, to list their equity shares on foreign stock exchanges in permissible jurisdictions. Sub-section (4) gives an exemption to these companies from complying with the rules mentioned in Section 89 (Declaration in Respect of Beneficial Interest in any Share), Section 90 (Investigation of beneficial ownership of shares), and Section 127 (Punishment for failure to distribute dividends). The purpose of these changes is to provide regulations for companies incorporated in India to directly list their equity shares on foreign stock exchange. It is anticipated that this amendment will enable Indian companies to raise funds directly through the foreign capital market, eventually, this will help Indian companies access global capital, improving the country's business environment and ease of doing business.

IV. THE ANALYSIS OF THE AMENDMENT

The increase in cases of money laundering that was done by the use of depository receipts was on a rise. On the other hand the companies did not even actively participate in the listing of shares through ADR/GDR route. As already stated, according to Prime Database, between 2008 and 2018, 109 companies raised Rs 51,847.72 crore through the ADRs/GDRs route. After 2018, none of the companies got listed overseas.¹⁷ This gives us an idea that the Indian Companies faced difficulty in listing their equity shares abroad.

¹⁶ Companies Act, Act, 2013, § 23, No. 29, Acts of Parliament, 2013 (India).

¹⁷ Hitesh, *supra* note 4.

ADR, GDR issues by Indian companies			
YEAR	NO.	AMOUNT (USD mn)	AMOUNT (Rs.crore)
2008	16	489.76	1,982.17
2009	25	3,720.33	17,851.82
2010	38	1,174.03	5,366.23
2011	19	553.50	2,531.71
2012	4	161.88	899.08
2013	2	40.00	219.39
2014	1	45.22	285.16
2015	2	1,595.72	9,872.01
2016	1	59.94	399.25
2017	-	-	-
2018	1	1,820.00	12,440.90
2019	-	-	-
2020	-	-	-
2021	-	-	-
2022	-	-	-
2023 (Till Oct,23)	-	-	-

Source: Prime Database

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Direct listing is much more beneficial in comparison to the traditional method of depository receipt. When it comes to ADR, in order to register the it, the depository bank and the non-US business whose equity shares are deposited need to file a registration statement on the SEC's Form F-6. It is necessary to submit a separate application to the relevant stock exchange or NASDAQ in order to list ADRs on one of these platforms. Listing standards vary across the American Stock Exchange, New York Stock Exchange (NYSE), and National Association of Securities Dealers Automated Quotations (NASDAQ), with the NYSE having the strictest restrictions and the NASDAQ having the loosest. For example, in order to list equity securities, a non-US issuer must meet the requirements set out by NYSE.

- (i) 5,000 or more owners globally, each of which owns at least 100 shares,
- (ii) at least 2.5 million shares that are traded openly,
- (iii) a publicly traded share market value of at least \$100 million globally,
- (iv) net physical assets with a global worth of at least \$100 million, and
- (v) a total pre-tax income of at least \$100 million during the previous three years, with at least \$25 in any of the three years.¹⁹

And likewise to list in any other stock exchange the use of GDR is predominant. The stock is

¹⁸ *Id.*

¹⁹ Mahim Raj, *American Depositary Receipts: Regulations in US and India*, 7 IJLA 62-76 (2011).

listed in the foreign jurisdiction by the use of GDR. Meaning thereby the use of Depository Receipts is essential whereby a custodian bank converts its equity shares in the into depository receipts and makes then it is available to the foreign investor. Hence, these banks act as underwriters (whereby the custodian banks or any other financial institution act as an underwriter).

So when it comes to direct listing these complexities are done away with. Direct listing allows Indian companies to list on foreign stock exchanges without issuing new shares or raising capital from its investor. Furthermore, it also allows the companies to directly list in foreign stock exchange without going for traditional IPO method.

(A) The remarkable case of Spotify

The remark here must be made of Spotify which directly listed its equity shares in the New York Stock Exchange (NYSE).²⁰ The SEC received a registration statement from Spotify first.²¹ Subsequently, the NYSE modified its listing requirements regulations to allow direct listings.²² The reason for which Spotify opted for a direct listing mechanism is because it allows the company to achieve market creation and financial stability.

Firstly, it allows the companies to provide liquidity without dilution that arises due to new security offering hence the existing shares directly come to the market and the shares held by the shareholders are not diluted.

Secondly, the underwriter fee is very high and in the case of direct listing, there is no need to pay an amount to the underwriter for incurring the risk of holding the equity shares on their books.

Furthermore, there is no lockup period for current shareholders. Instead, current owners of the issuer may easily sell their shares in accordance with the policies of a national market.²³

In addition, Spotify spent almost 46 million. Because there was no definitive commitment spread fee, Spotify was able to go public at around one-third of the cost of an IPO comparable to it.²⁴

²⁰ Benjamin J. Nickerson, *The Underlying Underwriter: An Analysis of the Spotify Direct Listing*, THE UNIVERSITY OF CHICAGO LAW REVIEW (Jan. 26 2014) <https://lawreview.uchicago.edu/print-archive/underlying-underwriter-analysis-spotify-direct-listing>.

²¹ Spotify Technology S.A., Amendment No. 3 to Form F-1 Registration Statement (Mar. 23, 2018), archived at <http://perma.cc/ES4F-D9YW>.

²² Securities and Exchange Commission Release No. 34-82627, 83 Fed. Reg. 5650 (Feb. 2, 2018) (amending § 102.01B of the NYSE Listed Company Manual).

²³ Benjamin, *supra* note 19.

²⁴ J.P. Morgan, Corporate Finance Advisory Trending Topics: A 1H 2018 Compendium no. 14 (Apr. 16, 2018), <http://perma.cc/X3L2-UW3T>.

(B) Potential Benefits

There are many benefits that a company could gain when it opts for direct listing. So, as far as Indian companies are concerned, the direct listing process is likely to be very beneficial not only for Indian companies but also for the Indian economy.

As we know there had been no overseas investment after 2018, through ADRs /GDRs and hence it has not contributed to the economic growth as well. To search for an intermediary was a time-consuming process. Due to this as well the companies avoided this route. Hence, the direct listing will be beneficial:

- (i) it will increase the competitiveness of the companies.
- (ii) Further, the companies will have a larger investment base and
- (iii) It will also have a better valuation for the companies.
- (iv) Startups, unicorns, and tech companies would also get more capital.

This would also in return increase the governance of the companies.

(C) The challenges involved

However, there is no clarity in the amendment. It is still not clear as to which companies would the new amendment be applicable to. Firstly, Section 23(3) of the Act says that the provision will be applicable on classes of “classes of company. However, the type of companies on which it will be applicable is still not clear. Furthermore, there is no regulatory framework regarding the same. The expert committee report has also stressed on the amendment of Indian regulatory frameworks such as the Foreign Exchange Management Act, 1999, and the Companies (Prospectus and Allotment of Securities) Rules 2014.²⁵ The two regulations at present talk about the issuance of Indian equity shares outside India through ADRs/ GDRs. However, there is no regulatory framework regarding direct listing of equity shares in foreign jurisdictions.

Currently, people resident outside India are able to subscribe to, buy, and sell capital instruments of companies established in India (as listed in schedule 1) under regulation 5(1) of FEMA 20R.²⁶ However, as of now, FEMA does not expressly address the issuance of equity shares to a resident of a country other than India by an Indian-incorporated company that is listed on a foreign stock exchange. So the Expert Committee of 2018, recommended adding part B to Schedule 1 which would include the regulation regarding the purchase/ sale of capital

²⁵ *Supra* note 2.

²⁶ Foreign Exchange Management Act § 5(1), Notification No. FEMA 20(R)/2017-RB (Reserve Bank of India 2017).

instruments on a recognized Stock Exchange outside India.²⁷ However, there is no regulatory framework regarding the same.

Secondly, the committee²⁸ also recommended for the change in Companies (Prospectus and Allotment of Securities) Rules 2014. It also suggests that the MCA should issue a notification, clarifying among other things that Chapter III of the Companies Act and related rules will not apply to listing of equity shares of companies incorporated in India on foreign stock exchanges. This will enable the framework for listing of equity shares of companies incorporated in India on foreign stock exchanges.²⁹

Hence, in the absence of such regulation, the MCA's amendment may pose challenges in the direct listing of shares in the foreign stock exchange.

V. CONCLUSION

The conventional ADR/ GDR route posed many obstacles in the path of the Indian companies to list their equity shares in the foreign stock exchange. There had to be many compliances that had to be fulfilled before listing itself. Companies engaged in corrupt practices were identified by SEBI, which has always kept an eye on them. In such circumstances, the notification regarding the direct listing of companies in the foreign stock exchange is indeed beneficial for both the Indian companies and the Indian economy. There had been many companies who were willing to list its shares in the foreign jurisdiction but were unable to do the same because of the lengthy process of searching an underwriter and converting their shares into depository receipts. However, the notification still lacks clarity about what kind of companies would be allowed to list their shares ultimately in the foreign stock exchange. Further, there is no regulatory framework till now that would govern the direct listing of shares in the foreign jurisdiction. There must be some amendment to the Foreign Exchange Management Act, 1999 and Companies (Prospectus and Allotment of Securities) Rules 2014 so that there is some clarity regarding the direct listing and its process.

In summary, even if it would broaden the pool of investors, the announcement is essentially a seal of approval in the lack of any regulatory framework.

²⁷ *Supra* note 2.

²⁸ *Ibid* 2.

²⁹ *Supra* note 2.