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Reverse Book Building Process under the New Delisting Regulations, 2021

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ABSTRACT

With the advent of COVID-19, the unpredictability of the stock market also continued to prevail in India with many small and big companies like Hexaware Technologies, Adani Power, Modern India Limited, Vedanta, etc. getting voluntarily delisted from the Stock Exchange. The reason for triggering voluntary delisting can be numerous other than the non-profitability of the company and therefore, the Securities and Exchange Board of India (SEBI) governs the delisting of companies under the SEBI (Delisting of Equity Shares) Regulation, 2009 which has now become the SEBI (Delisting of Equity Shares) Regulations, 2021 for providing a smooth and substantive governed process to the companies.

The basic intend of SEBI on introducing a new regulation altogether was to 'Time Bound' the entire process of delisting of equity shares as under the erstwhile regulations, there were no proper durations of executions because of which many delisting offers have failed in the past like that of Vedanta. As a result of lack of proper time-bound durations, the offer used to delay in time which used to be followed up by a change in market conditions and eventually would result in the failure of the delisting process. Therefore, the new regulations have laid much emphasis on mandating specific time boundations for the effective functioning of the delisting process.

In this article, we are going to understand the evolution and critically analyze the Reverse Book Building Mechanism as per the new Delisting Regulations of 2021 which is required to determine the discovered price of the purchase of shares to successfully delist the company.

Keywords: *Delisting Regulation, 2021; Reverse Book Building Process; Securities and Exchange Board of India (SEBI).*

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I. INTRODUCTION

On June 11, 2021, the Securities and Exchange Board of India put forth the SEBI (Delisting of Equity Shares) Regulations, 2021.³ These regulations were enacted to supersede the erstwhile delisting regulation which was named SEBI (Delisting of Equity Shares) Regulation, 2009 for the reason of making the process of delisting more transparent, efficient, investor friendly, robust, and time-bound in nature.⁴

Listing of the companies in the stock exchanges provides an opportunity for the companies to freely market and transfer their shares to the public. A company might want to get listed because of various reasons like greater shareholder's base, low cost of capital production, increase in prestige, high liquidity in shares trading, etc. There are more than 9000 companies that are listed in different stock exchanges in India, out of which a great portion of companies serves no purpose from being listed as there is a lack of active trading taking place in such companies. For such companies, the benefits derived from being listed in the stock exchange underweights the cost of listing, the heavy compliance requirements of SEBI as well as the disciplinary actions and penalties which are attracted in cases of non-compliance. Therefore, to meet the economic viability of the company as well as to provide an attractive and easy exit opportunity for the shareholders the delisting regulations streamline the appropriate process under the law.

-To delist the companies from the stock exchanges, the promoters or the acquirer has to obtain at least 90% of the total shares of the company. Therefore, the acquirer or the promoter buys these shares from the other shareholders of the company at a price that is decided by the way of a specified process known as the Reverse Book Building Process. The Reverse Book Building (RBB) is one of the most important aspects of the SEBI (Delisting of Equity Shares) Regulations, 2021 by the means of which the offer price (Now, Discovered Price) of the shares is determined for facilitating the delisting process.

Therefore, the Reverse Book Building can be defined as a mechanism by the way of which the acquirer or the promoters of the company offers the shareholders to buy back their stakes or shares in the company. The process of Reverse Book Building (RBB) is comparatively similar to that of a Book Building, the only difference is that the bidding is done by the shareholders. We will be discussing the whole process of bidding and RBB in the latter part of the article as

³ 227507.pdf, , <https://egazette.nic.in/WriteReadData/2021/227507.pdf> (last visited Jul 1, 2021).

⁴ SEBI | SEBI (Delisting of Equity Shares) Regulations, 2009 [Last amended on March 6, 2017], https://www.sebi.gov.in/legal/regulations/jun-2009/sebi-delisting-of-equity-shares-regulations-2009-last-amended-on-march-6-2017-_34625.html (last visited Jul 1, 2021).

we proceed.

II. RELEVANCE OF REVERSE BOOK BUILDING

The Reverse Book Building process is an extremely relevant part of the delisting process as upon its proper execution can only the shares be purchased by the acquirer and the promoter. There are many cases where a company must follow the Reverse Book Building process. Some of these cases are as follows-⁵

- In cases, where the promoters and founders of the company are willing to delist their company voluntarily because of non-trading activity and huge compliances, which makes it easier for the company to survive by the means of delisting itself will require the Reverse Book Building as an integral part of their delisting process.
- In cases, whereby the means of mergers or acquisitions, the total shareholding of the public shareholdings in a company falls below the minimum mandatory limit which is specified in the SEBI (Listing Obligations and Disclosure Requirements) Regulations or any listing agreements will also require Reverse Book Building as an integral part to facilitate their delisting.
- In cases, where the company is directed by the stock exchanges or Securities and Exchange Board of India (SEBI) for compulsory delisting of the company under the regulation. In such cases also, the discovered price is determined by the way of the Reverse Book Building process only.
- The Reverse Book Building process is also required in cases where the promoter or any person in the management has resulted in a fall of public shareholdings in the company below the specified limits of SEBI (LODR) Regulations because of consolidation of his holdings in the company.

III. COMPARATIVE EVOLUTION OF REVERSE BOOK BUILDING PROCESS

(A) Reverse Book Building Process in SEBI (Delisting Of Equity Shares) Regulation, 2009

According to the 2009 regulation, the delisting process would start from the promoter or the founders who are required to appoint a Trading Member and nominate a Merchant Banker. The company is then required to make a Public Announcement (PA) about the future delisting plans which is clubbed with an offer letter along with a bidding form to all the eligible public shareholders of the company at that time. All these documents are to be filed with the concerned

⁵ What is Reverse Book building – All you have to know about, , <https://caknowledge.com/reverse-book-building/> (last visited Jul 1, 2021).

stock exchanges without any delay in time. The stock exchange, in turn, updates the announcement thus made by the company to its website to make the shareholders aware of the starting of the delisting process.⁶

As per **Regulation 15** of the erstwhile regulations of 2009, the floor price (the price at which the promoters or the acquirers are willing to buy the shares) is fixed and the *Reverse Book Building Process* is initiated. It is to be noted that the floor price is determined and calculated under the **SEBI (Substantial Acquisition of Shares and Takeover) Regulations, 2011**. As per the following regulation, the calculation of floor price is done by the means of identifying the historic price for the prescribed look-back periods which starts from the announcement of a tender offer in a Public Announcement (PA).

After the fixation of the floor price, the public shareholders start entering with their respective bids during the bidding period. Eventually, after the auditing of the final bids, the offer price is discovered and the company has the ultimate right to accept or reject the offer price.

In case, the offer is accepted by the company, the merchant banker announces the acceptance along with the offer price of the purchase. According to **Regulation 21** of the erstwhile regulation, the remaining shareholders also have the right to tender their shares to the company at the same offer price within a year from the date of delisting.⁷

(B) SEBI (Delisting of Equity Shares) Regulations, 2009, (Amendment, 2015)

Based on the *Discussion Paper* issued by the Securities and Exchange Board of India in 2014,⁸ it was observed that the delisting offers were failing because of the rejection of the offer prices by the companies. Therefore, to curtail the shortcomings of the Reverse Book Building system a provision in **Regulation 17** was inserted making at least 25% participation mandatory for the Public Shareholders in the bidding process.

(C) SEBI (Delisting of Equity Shares) Regulations, 2009, (Amendment, 2018)

The amendments of 2015 did not prove to be of much success. Moreover, the Reverse Book Building process under **Regulation 8** did not take into consideration the book value of the concerned company. As a result, SEBI based on the *Discussion Paper* issued on July 26, 2018,⁹

⁶ Manal Shah, *Reverse Book Building Process in the Delisting Regulations - A Critique*, THE SECURITIES BLAWG (2020), <https://www.thesecuritiesblawg.in/post/reverse-book-building-process-in-the-delisting-regulations-a-critique> (last visited Jul 1, 2021).

⁷ *Id.*

⁸ 1399633833837.pdf, https://www.sebi.gov.in/sebi_data/attachdocs/1399633833837.pdf (last visited Jul 1, 2021).

⁹ SEBI | Discussion Paper on Delisting of Equity Shares Review of “Reverse Book Building Process,” https://www.sebi.gov.in/reports/reports/jul-2018/discussion-paper-on-delisting-of-equity-shares-review-of-reverse-book-building-process-_39712.html (last visited Jul 1, 2021).

highlighted the concerns over the Reverse Book Building Process and the thwarting of the genuine attempts of the companies in delisting. Therefore, SEBI passed an amendment, and a provision was inserted for the promotor's counter-offer to the biddings placed by the public shareholders. However, the provision of a counter-offer is also restrictive as the price thus determined by the promoter in a counter-offer cannot be less than the book value of the company concerned.

IV. SEBI (DELISTING OF EQUITY SHARES) REGULATIONS, 2021

The Reverse Book Building Process under the new regulations is provided in Chapter IV and contains the following new terms as per the new delisting regulations of 2021-

- The concept of floor price is unchanged and will be calculated in the same manner as it used to under the SEBI (SAST) Regulation, 2011. It is to be calculated on the reference date on which the stock exchanges were to be notified of the first (1st) Board Meeting in which delisting is considered.¹⁰
- While the concept of Floor Price is unchanged, a new concept of **INDICATIVE PRICE** is introduced for the first time in the new regulations even though it was already in practice in the market by many companies. Therefore, now the acquirer has a right to disclose an *Indicative Price* that shall be higher than the determined floor price to indicate the market about an acceptable range of price by the promoters or the acquirer. Moreover, the acquirer/promoters also have the right to increase such prices until the commencement of the bidding process.¹¹
- The term '**Exit Price**' has been replaced by the word '**Discovered Price**'. This discovered price is referred to as a price at which the shares which are accepted through the eligible bidding process make the acquirer's shareholding (along with Persons Acting in Concert) touch the threshold of 90% of the total issued shares through the Reverse Book Building Process.

According to the erstwhile regulations¹², an **Escrow Account** was used to open, and 100% of the total consideration was deposited by the promoters or the acquirers into that account. However, in the new delisting regulations, the process and RBB cycle for the acquirer have

¹⁰ SEBI | Securities and Exchange Board of India (Delisting of Equity Shares) Regulations, 2021, , https://www.sebi.gov.in/legal/regulations/jun-2021/securities-and-exchange-board-of-india-delisting-of-equity-shares-regulations-2021_50517.html (last visited Jul 1, 2021).

¹¹ Understanding SEBI's New Rules For Delisting Offers, , <https://www.bloomberquint.com/business/understanding-sebis-new-rules-for-delisting-offers> (last visited Jul 1, 2021).

¹² SEBI | SEBI (Delisting of Equity Shares) Regulations, 2009 [Last amended on March 6, 2017], *supra* note 2.

been changed. The *New Acquirer's Reverse Book Building Cycle*¹³ will contain the following steps to be fulfilled-

1. The acquirer within **7 working days** of the Shareholder's approval has to open an interest-bearing *Escrow Account* and deposit an amount **equal to 25%** of the total consideration.
2. Followed by a deposit of the remaining 75% of the total consideration before making the Detailed Public Announcement in the same *Escrow Account*. The following changes in the Escrow account are made to ensure a financial commitment from the acquirer's side.
3. After the deposits are made, the acquirer has to make a Detailed Public Announcement within 1 (One) working day from the date of the reception of the *In-Principle Approval* in 3 different newspapers.
4. After this, a specified date has to be fixed which shall **not be later than 1 working day** from the Detailed Public Announcement.
5. After the previous step, the *Letter of Offer* must be dispatched which shall be not done not later than **2 working days** from the date of *Detailed Public Announcement*.
6. As a final step, the Bidding Period shall start **not later than 7 working days** from the date of the *Detailed Public Announcement* and the period shall remain open for **5 Working Days**.

In addition to that, **REGULATION 21** of the New Delisting Regulation, 2021, which talks about the Minimum number of Equity Shares to be acquired by the Promoters or the acquirer to successfully delist the company has also changed. The provision under *Regulation 21* also includes 3 categories of shareholders exclusions from the total issued shares. These are-

1. Custodians against which depository receipts shares are issued overseas.
2. *ESOP* trusts are established for employee benefits.
3. Inactive shareholders

As a result, the outcome of the Reverse Book Building process has to be announced within **2 Hours of the closure** of the Bidding Period by the Merchant Banker, followed up by a **Public Announcement** regarding the failure or success of the RBB along with the disclosure of the **Discovered Price** within **2 working days from the closure** (Which was 5 working days in the erstwhile regulations).

Moreover, the concept of **Counter-Offer** has been retained by the regulations but the method

¹³ SEBI | Securities and Exchange Board of India (Delisting of Equity Shares) Regulations, 2021, *supra* note 9.

according to which the book value will be calculated has been properly stipulated in the new regulations which will be determined based on financial statements (both consolidated and standalone, whichever is higher).

V. CRITICAL ANALYSIS OF THE NEW DELISTING REGULATIONS, 2021

It is to be noted that the new regulations have been welcomed with open hands as it has provided various positive steps towards making delisting process easier and more time-bound. Changes like the requirement for a company for setting up of a committee of independent directors for reasoning out the recommendations for the delisting proposals, specified timelines for the performance of several steps during the process of delisting, providing a proper manner of calculation of the book value while calculating the counter-offer, etc. will prove to be very effective in future to make the whole process of delisting more efficient and fast.

However, according to the personal analysis of the authors, the new delisting regulations have again failed to mention the elephant in the room, or other words, it has failed to address the most common issue of deadlock between the shareholders and the acquirers. In order to have a detailed critical view of the new changes made, we have decided to analyze the provisions one by one-

(A) Floor Price

If the acquirer or the promoters wants to buy back the shares of the shareholders, then it will be more reasonable if the floor price is computed on the book value as it has been observed from various instances in the past that the floor price seldom represents the true value of the company and therefore, during the bidding process the deadlock between the acquirer and shareholders becomes a common ground of failure of the delisting proposal. In addition to it, SEBI shall look into the possibilities of computing the floor price considering the book value as it will safeguard both the acquirer as well as the shareholders and make the overall process of delisting more efficient. Moreover, other methods like the *Contingent Price Mechanism* can also be considered to rule out the adverse effect of the opportunistic behavior of the promoters.

(B) Indicative Price

Since the floor price usually doesn't reflect the true value of the company and is often much lower than the price at which the shareholders are willing to sell their shares, the *Indicative Value* also fails to serve any substantive purpose. In reality, the discovered price computed after the RBB is always much higher than the indicative price of the offer.

(C) Counter-Offer

The right of the counter-offer of the promotor is also restrictive and hence, cannot be made on a price that is lower than the present book value of the concerned listed company. It is a known fact that the price at Book Value is not always consistent and accurate in reflecting the actual representation of the valuation of the company because of which it might not prove to be profitable for both the parties and eventually result in the failure of the delisting offer.

VI. CONCLUSION

The SEBI (Delisting of Equity Shares) Regulations, 2021 has brought numerous changes in the whole process of delisting of companies in India which will eventually result in making the process of delisting more time-bound and efficient. But following the viewpoint of this article, the new regulations have not addressed the solutions for the major issue of the deadlock which is created between the shareholders and the acquirers concerning the calculation of discovered price. There have been numerous instances in the past in which the shareholders were found to form cartels to manipulate the biddings during the Reverse Book Building Process following which, it becomes a win-win situation from the side of the shareholders as if the acquirer will want to delist the company, he will buy the shares at a higher price as well as in cases where the delisting proposal fails, it has been observed that the share price of such companies rises inorganically which ultimately benefits the shareholders. Therefore, in a conclusion, it can be said that the new regulations have brought incomplete changes to benefit the whole process of getting a company delisted from the stock exchange.
