

Big bang changes to the SEBI ICDR Regulations

The Securities and Exchange Board of India (“SEBI”) had, in its board meeting held on September 30, 2022, approved certain key proposals, including: (i) introduction of pre-filing of offer document as an alternative mechanism for the purpose of an initial public offering (“IPO”), and (ii) disclosure of key performance indicators (“KPIs”) and price per share of the issuer company in public offering based on primary issuances and secondary transfers undertaken in the past. SEBI has now notified the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) (Fourth Amendment) Regulations, 2022 on November 21, 2022 (“ICDR Amendments”). Some of the key highlights of the ICDR Amendments are as follows:

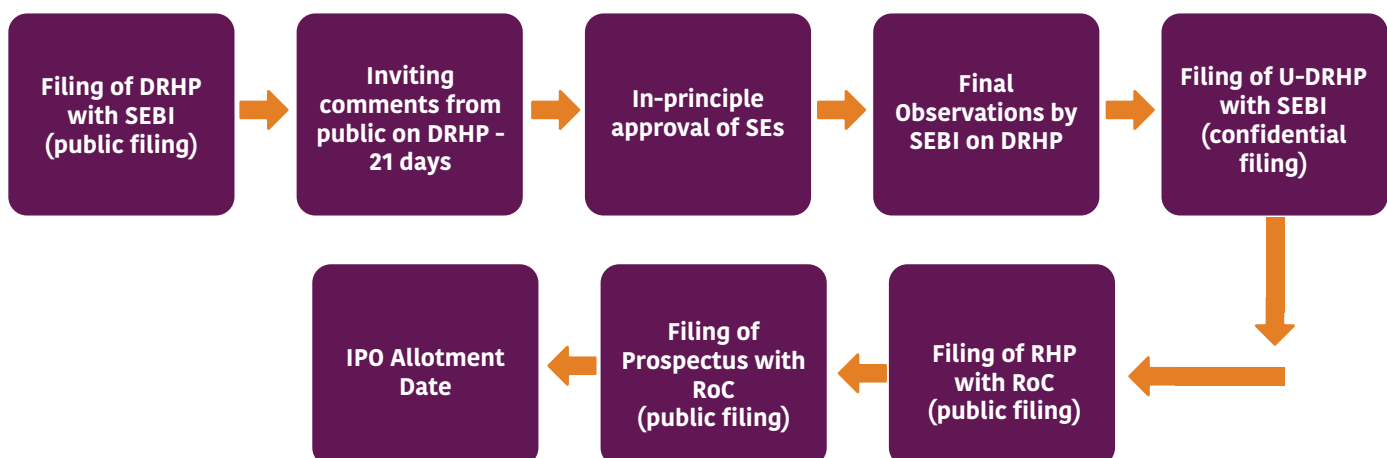
1. Introduction of Pre-Filing Process:

For IPOs listing on the main board, an alternative process has been introduced to facilitate public companies

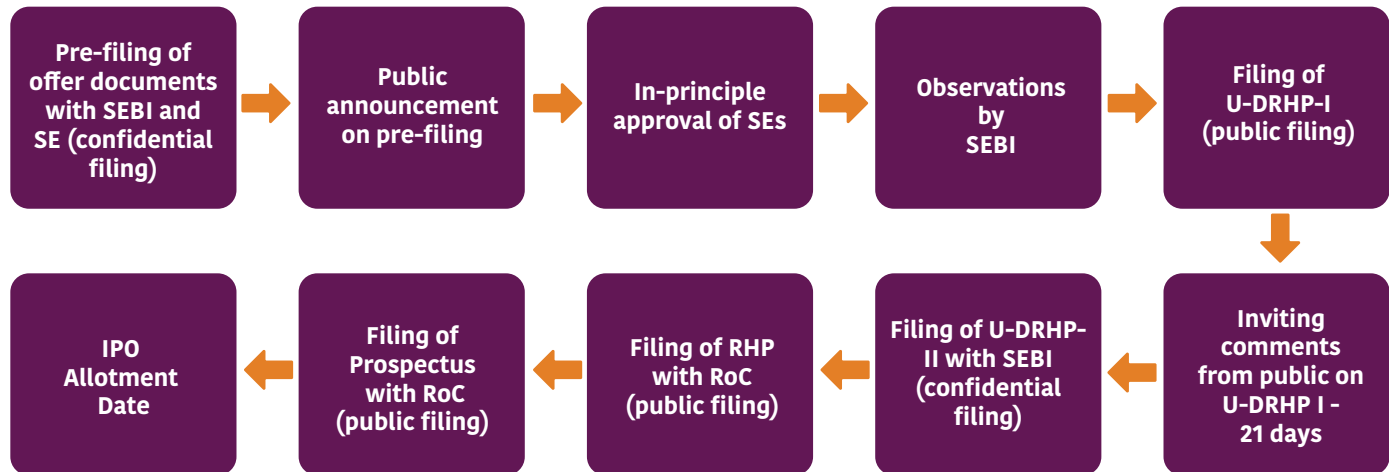
to file their draft offer document with SEBI and the stock exchanges on a confidential basis (“**Pre-Filed Document**”), and for which a new chapter (Chapter IIA) has been introduced to the SEBI ICDR Regulations. The benefits of this process include keeping commercially-sensitive information confidential up to the time that the issuers are very sure they want to go ahead with the transaction. It also now allows issuers and regulators to resolve disclosure-related concerns or any other complex matters relating to the issuer or its industry prior to the disclosure becoming public, and ensures that the document that is made available for public review incorporates the regulator’s inputs and observations.

The flow charts below provide an overview of the existing and the alternative process, and key points relating to the process:

Existing Process



Process under Chapter IIA pre-filing regime



In several ways, the pre-filing process and the filing/compliance related requirements in relation to a Pre-Filed Document are quite similar to the approach currently being followed. However, there are several notable deviations:

▮ Accompanying Documents (including DD Certificate)

In addition to the customary due diligence certificate of the lead managers, which are filed along with a regular DRHP, a Pre-Filed Document will also need to be accompanied with an undertaking from the issuer company and the lead manager that they will not conduct marketing or advertisement for the intended IPO (therefore, requiring all public communication to be in line with past practice). However, in an interesting and positive step, issuer companies will now be formally allowed to interact with qualified institutional buyers (“**QIBs**”) for the marketing of the IPO following the filing of Pre-Filed Document, basis information included in Pre-Filed Document. The issuer and lead managers will be required to prepare a list of QIBs who have participated in such interaction(s), and will also be required to submit to SEBI an intimation of completion of interaction with the QIBs (“**Limited Interaction Intimation**”). This change will require the issuer and the lead managers to put adequate controls in place to ensure that the contents of the Pre-Filed Document do not find their way in the public domain. Like in other jurisdictions, non-disclosure agreements may need to

be entered into prior to such meetings. This will also allow good feedback on the viability of the issue.

▮ Public Announcement

While the Pre-Filed Document will not be available in the public domain, the issuer company will be required to make public announcement disclosing the fact of such filing, without any other details, within two days of its filing.

▮ Receipt of Observations

Two additional prongs have been added for starting the 30-day clock to receive SEBI’s observations on the Pre-Filed Document i.e. (i) date of Limited Interaction Intimation, or (ii) date of intimation to SEBI about the conversion of outstanding convertible securities or exercise of any other right, which would entitle any person with any option to receive equity shares (not including any convertible securities or rights presently permitted under Regulation 5(2) of the ICDR Regulations). Depending on the deal dynamics, this has the potential of increasing the review process and issuance of observations on the Pre-Filed Document, whilst at the same time, providing issuers with more control on driving the process given the timelines of QIB interactions, etc., will be largely commercially driven.

7 Filing of U-DRHP I

The U-DRHP-I will be the first public filing of an offer document by the issuer, and as such will closely resemble a DRHP filing under Chapter II. Whilst the requirements in relation to submission of documents, public announcements, availability on websites, etc., are similar to the approach followed for regular DRHP filings under Chapter II, an interesting change now is the introduction of a ‘cool-off’ period of seven working days between the QIB interactions and the filing of the U-DRHP-I. A U-DRHP-I will be available for comments from public for at least 21 days from the date of filing. The publicity restrictions that apply post DRHP filing under a Chapter II filing, shall now become applicable from the date of filing of the U-DRHP-I. Arguably, whilst not explicit in the ICDR Amendments, the timing of release of research reports is also likely to be linked to the filing of U-DRHP-I.

7 Filing of U-DRHP II

Post 21 days, the lead managers will submit to SEBI details of comments received and consequent changes made to the document. Analogous to the customary approach of an updated draft red herring prospectus filing today under Chapter II, the submission of a second updated draft offer document (“**U-DRHP-II**”) will be required to be made with SEBI prior to filing of red herring prospectus with Registrar of Companies (“**RHP**”). The ICDR Amendments are silent on situations where the issuer or lead managers continue to receive complaints (frivolous or otherwise) post the expiry of the 21-days period.

7 Increased flexibility to undertake changes to the capital structure, issue structure and significant relaxations in variation of objects of the fresh issue

Whilst the Chapter IIA regime has been introduced, SEBI appears to be cognisant of the fact that the Pre-Filed Document may be filed at a stage even when certain aspects of the issue are not fully concrete. As such, until SEBI issues observations on the Pre-Filed Document, the issuer company will be permitted to -
(i) Continue with convertibles/ options: This would pertain to outstanding convertible securities and any other right to receive equity shares of the issuer company, not including any permitted ESOPs or fully paid up outstanding convertible securities, which may



continue to be held as per Regulation 5(2) of the SEBI ICDR Regulations; and **(ii) issue specified securities and convertibles:** Issuance of specified securities, and securities that are compulsorily convertible at the time of filing of the RHP, with details in relation to the maximum number of equity shares to which such convertible securities shall convert being provided in the U-DRHP-I. The issuer is also permitted to undertake significant changes to the issue structure (to the extent of 50% of the fresh issue, as opposed to the 20% permitted under the Chapter II regime) and objects of the fresh issue (to the extent of 50% in certain situations as compared to 20% under the existing regime). Post filing of the U-DRHP-I the existing refiling triggers applicable to Chapter II filings shall apply. In another welcome amendment, the requirements in relation to testing the eligibility of securities for offer for sale (“**OFS**”) or promoter contribution are only applicable at the time of filing of the U-DRHP-I and not at the time of filing of the Pre-Filed Document. This will provide issuers with the flexibility of filing a Pre-Filed Document without necessarily waiting for conditions for OFS or for meeting promoter contributions.

7 Increased validity of observations

The Chapter II regime allows for an issuer to open a public issue for subscription within 18 months from the date of SEBI observations on the Pre-Filed Document, provided that the U-DRHP-I is filed within 16 months from the date of SEBI observations. The existing regime provided for SEBI’s final observations on the DRHP, which would remain valid for a period of 12 months.

2. Disclosure of Key Performance Indicators (“KPIs”) and Past Price Information in the Basis for Issue Price section:

The ICDR Amendments have now formalised the inclusion and relevance of KPIs as a significant factor for determining the issue price in all IPOs. Similarly, the ICDR Amendments now necessitate the comparison of the IPO price with the pre-IPO price of shares in primary/ secondary transactions. Interestingly, these requirements will apply to all IPOs (including ongoing IPOs) where the red herring prospectus is being filed after the notification of the ICDR Amendments.

i. Disclosure of KPIs

For all the KPIs which are disclosed in the offer document, the issuer companies and the lead managers are required to ensure the following:

▮ Time-period of KPI disclosures

For the ‘Basis for Issue Price’ section, the ICDR Amendments mandate the disclosure of all KPIs pertaining to the issuer that have been disclosed to investors at any point during the three years preceding the date of filing of the DRHP/ RHP. At the same time, the ICDR Amendments also require that for each KPI being disclosed in the offer document, the details are provided for a period which is co-terminus with the period for which the restated financial information is disclosed in the offer document.

▮ Qualitative disclosures for KPIs

All KPIs disclosed in the offer document are required to be comprehensive, replete with the explanation of the historical use of such KPIs by the management to analyse, track and monitor the operational and financial performance of the issuer. Similarly, if there have been any additions or dispositions to the business over time, a comparison of the KPIs is required to be done and explained. Further, if there are any additional material KPIs which have a bearing on the basis for issue price, the same may also be disclosed by the issuer and lead managers.

▮ Approval and certification requirements

The KPIs disclosed in the offer document (and disclosed by the issuer, post-listing) will be

required to be certified by the statutory auditor(s) or peer reviewed by chartered accountants or cost accountants. The ICDR Amendments also require the KPIs to be approved by the audit committee of the issuer.

▮ Comparison with peers

For the KPIs included in ‘Basis for Issue Price’ section, the disclosure of comparison with Indian-listed peers or global-listed peers of a comparable size, from the same industry and with similar business model is now mandatory. Whilst there is provision to explain differences if a one-to-one comparison with a peer is not possible, it will be interesting to see this requirement play out considering the wide range of business models adopted by companies, especially the new-age technology companies.

▮ Post-listing disclosure of KPIs

The KPIs to be disclosed in ‘Basis for Issue Price’ section at least once in a year (or for any lesser period as determined by the issuer company), for a duration that is at least the later of (i) one year after the listing date or period specified by SEBI; or (ii) until the utilisation of the issue proceeds. Any change in these KPIs during such period will need to be explained. Whilst this was a well understood norm, companies have not been very forthcoming with such disclosures, which has forced SEBI to codify it. This will ensure better compliance.

ii. Disclosure of Past Price Information

The following disclosures in respect of primary and secondary transactions preceding the filing of the DRHP/ RHP are now required to be included in the ‘Basis for Issue Price’ section.

▮ Price per share based on

- primary issuance of shares (equity or convertible securities) in the 18 months preceding the date of filing of the DRHP / RHP, excluding shares issued pursuant to employee stock option scheme and bonus issue, or
- secondary sale / acquisition of shares (equity or convertible securities) in the 18 months preceding the date of filing of the DRHP / RHP, where the

promoter / promoter group entities or selling shareholders in IPO or shareholder(s) having the right to nominate director(s) on the board of directors of the issuer company are a party to the transaction (excluding gifts).

In another welcome move, the disclosures are only required where such issuance, sale or acquisition is equal to or more than 5% of the fully diluted paid-up share capital of the issuer company (calculated on the basis of the pre-issue capital before such transaction(s) and excluding employee stock options granted but not vested), in a single transaction or multiple transactions combined together over a span of rolling 30 days. Further, the disclosed price per share is required to be adjusted for corporate actions including split, bonus, etc., undertaken by the issuer company.

- 7 In case there are no such transactions in the last 18 months, then the information on the basis of last five primary or secondary transactions, not older than three years prior to the date of filing of the DRHP / RHP, irrespective of the size of transactions.
- 7 The disclosures will also include the comparison of the floor price and cap price in the IPO against the weighted average cost of acquisition (“**WACA**”) based on primary or secondary transaction(s) summarised above. Along with the WACA comparison, the disclosures will also include comparison of the KPIs and financials ratios for the last three full financial years and stub period (if any), as well as external factors which may have influenced the IPO price.
- 7 The price band advertisement will now include the WACA comparison against the floor/ cap price (under the ‘Risk to Investors’ section), and also a recommendation of a committee of independent directors stating that the price band is justified based on quantitative factors / KPIs disclosed in ‘Basis for Issue Price’ section vis-à-vis the WACA of primary issuance / secondary transactions disclosed in ‘Basis for Issue Price’ section.

3. Other key amendments:

In addition to the introduction of the pre-filing regime and additional disclosure requirements for



the determination of basis of issue price, the ICDR Amendments have also introduced a few other key changes, including (i) removal of the flexibility of filing of offer documents with the regional office of SEBI for IPOs, rights issues and further public offerings; and (ii) requirement of appointment of a monitoring agency for preferential issues and qualified institutional placement.

Afterword

The latest round of amendments to the ICDR Regulations marks a substantial shift in the manner in which capital will be raised through the IPO route in India, going forward. The introduction of a pre-filing regime, which has been tried and tested successfully in several overseas jurisdictions for some time now, is a testament to the maturity of Indian capital markets, and will go a long way in making the capital raising process attractive to all types of issuers. In the west, pre-filing has proven to be a win-win formulation for regulators and issuers, and the Indian story will hopefully follow suit.

The changes proposed vis-à-vis determination of IPO pricing are, in many ways, a product of their time and environment – furthering the overarching and constant objective of the regulator to make disclosures more robust, and to protect the interests of the investors. Once the creases are ironed out based on dialogue with the market participants and intermediaries, teething troubles aside, this will prove to be a step in the positive direction in the long run.

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