Mandatory listing of non-convertible debt securities by listed entities

28 September 2023

***Partner**: Pranav Sharma and Mallika Chopra, **Counsel**: Aditi Bagri*

1 Background

In its board meeting of 28 June 2023 (**Board Meeting**), the Securities and Exchange Board of India (**SEBI**) approved the mandatory listing of non-convertible debt securities (**NCDS**) by listed issuers having outstanding listed NCDS, with effect from 1 January 2024. (To read our earlier update on this development, click here.)

Consequently, SEBI amended the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (**LODR Regulations**) on and with effect from 19 September 2023.

The aforesaid amendments are aimed at:

a. facilitating better transparency in price discovery;

b. avoiding undesirable opacity in the corporate bond market on account of information asymmetry across listed and unlisted NCDS; and

c. addressing concerns of mis-selling of unlisted securities and preventing arbitrage due to price differences between listed and unlisted International Securities Identification Numbers (ISIN).

Listed entities that have listed non-convertible debt securities outstanding after 1 January 2024 and that propose to issue non-convertible debt securities thereafter, are now mandated by SEBI to undertake only listed issuances for such non-convertible debt securities, subject to certain exceptions and conditions. This update highlights the key amendments prescribed by SEBI to give effect to this decision.

2 Key amendments

The key amendments to the LODR Regulations are:

a. NCDS issued by a listed entity on or after 1 January 2024 (**Cut Off Date**), where such listed entity has outstanding listed NCDS, must be listed;

b. NCDS issued as of 31 December 2023 (including unlisted NCDS issued on or after such amendments) by a listed entity having outstanding listed NCDS may be optionally (and not mandatorily) listed;

c. where a listed entity is proposing to issue listed NCDS on date '*X*' falling on or after the Cut Off Date, all outstanding unlisted NCDS issued by that listed entity on or after the Cut Off Date but before '*X*' must be listed within three months from '*X*'.

The following classes of securities have been exempted from compliance with these requirements:

a. long term capital gains tax exemption bonds issued under Section 54EC of the Income Tax Act, 1961;

b. NCDS issued in terms of an agreement between the listed issuer and multilateral financial institutions (**MFI**);

c. NCDS issued pursuant to an order of any court or tribunal or any regulatory requirement stipulated by a financial sector regulator.

The latter two are subject to the conditions that the NCDS must be locked-in and held to maturity by the original holders and must be unencumbered. Additional disclosures are also to be made to the stock exchanges by the listed entities proposing to issue NCDS further to the exemptions listed above.

3 Impact of the amendments

These amendments are likely to have the following impact on the debt market:

a. Effective from the Cut Off Date, any issuance of NCDS by a listed entity having outstanding listed NCDS will have to be a listed one. Therefore, if a listed entity having outstanding listed NCDS proposes to issue unlisted NCDS after the Cut Off Date, it will have to either: (i) delist all its outstanding listed NCDS, or (ii) redeem the outstanding listed NCDS in full, in each case, before issuing unlisted NCDS after the Cut Off Date.

   The key challenge with the first option of voluntarily delisting the listed NCDS is that the issuer will require the consent of 100% of the NCDS holders. On the other hand, adoption of the second option will be subject to the terms of the relevant issuance and will also depend on the tenor of the instrument and related regulatory considerations – such as minimum maturity conditions applicable in case of investments made under the foreign portfolio investment route or the exercise of a put or call option prior to the expiry of one year of the issuance.

b. The exemption provided in the amendments is only applicable to MFIs (and not any other class of investors), subject to certain conditions. In order to take the benefit of the exemption, MFIs are under a hold-to-maturity obligation (with *inter se* transfers amongst MFIs also not being permitted). These restrictions seem onerous and will make investments in unlisted NCDS unattractive for MFIs. Additionally, the condition relating to the regulatory lock-in and any related mandatory filing requirements remain subject to further clarifications from SEBI.

c. Since it is mandatory to have listed NCDS rated, all unlisted issuances that are required to be listed as a consequence of the amendments will also need to be rated. The operational aspects of the transition from unlisted NCDS to listed NCDS are unclear at this stage and will require further clarifications to facilitate such listing uniformly, particularly since all listed NCDS above a prescribed threshold are required to be issued through the electronic bidding platform.

The amendments are a positive move insofar as they seek to enhance transparency. However, a consequent and larger impact could be a delisting of several listed NCDS (subject to end-use conditions applicable at the time of issuing such NCDS) resulting in an even more illiquid secondary corporate bond market. Clarifications from SEBI, the stock exchanges and the depositories on the process for listing previously issued unlisted NCDS are awaited before issuers can take a definitive view on their short-term and medium-term fund-raising plans.