



Direct Listing of Shares – A Sure Way of Unlocking Hidden Treasures

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This article tries to find a new and positive approach for listing of shares of an unlisted company without opting to public or merging with yet another entity for the sake of listing status.

INTRODUCTION

Listing and trading in shares would enable to unlock the value of the investment resulting in wealth creation and its realization for its owners. There are two ways to get shares of an unlisted company listed on a Stock Exchange.

1. Initial Public Offer

Public issue of shares helps in unlocking the pre-public issue shares held by promoters and other shareholders.

2. Merging the unlisted company with a listed company

This is a sure way of getting the shares of the unlisted company listed on the stock exchange but valuations of shares will be critical issue.

There are certain conditions for any company to go public. The SEBI (Disclosures and Investor Protection) Guidelines provides pre-conditions as eligibility criteria for a company to go public. The only two designated stock exchanges in India being National Stock Exchange and Bombay Stock Exchange also impose strict conditions as to capital and turnover as bench mark for listing. All these conditions, though very much warranted, do pose considerable difficulties to the business houses that are fundamentally very strong and having fabulous intrinsic value for their shares to approach any of the Stock Exchanges for listing of their shares. The cost of an IPO which is about 10 to 12% of the money that would get raised is also prohibitive for such enterprises.

Few reasons why small but high intrinsic value companies do not venture to go public are:

1. Cost associated with an IPO is prohibitive.
2. Too many intermediaries involved in the public issue of shares.
3. Extensive procedure of compliance
4. Too much of time is wasted in processing an IPO
5. Fear of failure.

To avoid going to public, small companies seek capital from venture capitalists, high net worth individuals, promoters bringing in their own money, Bank loans, etc. Such capital is short sighted and generally helps the company to overcome the situations temporarily. Over a period of time, the money so raised may burden the company thereby bringing down its efficiency level. That apart, the valuation of shares is not realistic and liquidation of shares is almost zero.

Few more valid reasons as to why unlisted companies do not wish to go public are:

1. they don't require the kind of additional capital they may be required to be raised through an IPO
2. servicing the additional shareholders would be costly and uneconomical
3. fear of unknown people getting control over the company they nurtured for years

Though on text these reasons look unfounded, in reality there are many sad stories to substantiate them.

Of late SEBI is taking several steps to quicken the processing of IPO, amending rules pertaining to Retail shareholders, High Net worth Shareholders, Qualified Institutional Bidders etc. Recently SEBI had allowed promoters to increase their holdings to a maximum of 75% and now after the

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recent Corporate events, SEBI is looking to amend even the Take Over Guidelines to assist 'Market' to find its realistic state and help shareholders. Similarly, it is time now for SEBI and the Stock Exchanges to ease the listing norms and to allow the public unlisted companies to directly list their shares with the Stock Exchanges without the need to go for a public issue. SEBI will do well to allow 'direct listing' of shares by such eligible companies.

The concept of 'direct listing' is not new. Even our neighboring country, Bangladesh has introduced direct listing of shares at Dhaka Stock Exchange by way of a Regulation introduced in 2006. About half a dozen companies in Bangladesh have got listed their shares through direct listing. All without going for an IPO! Direct listing of shares is also available with Euronext. This is being discussed seriously in few other countries as an effective alternative to IPO route of listing shares.

The idea here is that public unlisted companies having a certain number of years of existence, having certain amount of capital, a minimum fixed number of shareholders, availability of shares in electronic mode, be allowed to get their shares listed either at NSE or at BSE. Such an option would allow unlocking the value of billions of worth securities. An appropriate Regulation needs to be introduced by the SEBI to ensure proper utilization of the option.

Some of the requirements to consider a company to be eligible for 'direct listing' of its shares could be :

The concerned company –

1. shall be in existence for a minimum of 7 years as on the date of application for Direct Listing ;
2. shall have minimum paid up capital – say Rs. 10 crores ;
3. shall have no accumulated loss ;
4. shall be in commercial operation for at least five immediate previous years ;
5. shall have profit in three years out of the immediate last five completed accounting/financial years with steady growth pattern ;
6. is regular in holding annual general meeting (AGM) ;
7. shall have a Board in line with Clause 49 of the listing agreement ;
8. has a high level of Corporate Governance with reference to transparency in Financial and other details ;
9. the intrinsic value of the shares is very high – say a minimum of 5 times of its face value.

The desiring companies should be made to apply to the designated stock exchanges, along with the documents such as:

1. Copy of the Board Resolution recommending seeking listing with the Stock Exchange/s.
2. Copy of the Members' Resolution recommending applying for listing with the Stock Exchange/s.
3. Copy of the Members' Resolution approving amendment to the Memorandum and Articles of Association of the Company.
4. Updated copy of the Memorandum and Articles of Association along with documents evidencing having filed with the ROC.

5. A Corporate Governance Compliance Certificate issued by a Practising Company Secretary.
6. A Certificate by a Practising Company Secretary confirming compliance of all listing requirements by the company.
7. Apart from the above, the company seeking direct listing should file with the SEBI and the Stock Exchange a detailed document much in the lines of our current Prospectus or Red Herring Prospectus.

INTERMEDIARIES TO BE INVOLVED

1. Merchant Banker: Merchant banker may be required to prepare the offer document, much in line with the preparation of a prospectus of the company. A merchant banker should be required to represent the issuer to the SEBI and Stock Exchange.

2. Legal Advisor : The legal advisor should go through all the pending legal cases, agreements and contracts and certify accordingly.

3. Statutory Auditor should be required to certify the fair and correctness of the accounts.

4. Depository Participants : The company desiring to have its shares listed at the Stock Exchange should have its shares compulsorily in electronic mode. The company should have entered into the tripartite agreement with both the Depositories ie., NSDL and CDSL. A certificate should be obtained from each of the Depositories confirming that the shares of the subject company are available under demat and the same should be submitted to Stock Exchange.

5. Share Transfer Agent : The company would be required to appoint a Share Transfer Agent to handle both physical and electronic data of shareholders. Copy of the Agreement with the Share Transfer Agent should be submitted to Stock Exchange.

LISTING COMMITTEE

Similar to the Committee set up to arrive at the "Basis of Allotment" in an IPO, SEBI may constitute a Committee wherein the representatives of SEBI, Stock Exchange, the Company, Depositories, Registrars and the Public are members who would evaluate the application made by the Company and if fully satisfied recommend to the Stock Exchanges for listing and to allow trading in the shares of such companies. SEBI would do well to define the role and responsibilities of such a Committee and also provide appropriate time lines to avoid undue delay in arriving at a decision by the Committee.

CONCLUSION

A detailed study could be done by SEBI on such unlisted companies which, if given an opportunity of direct listing would be willing to accept it. SEBI could invite the practising company secretaries, chartered accountants and even Merchant Bankers to provide data on such companies being serviced by them. It is felt that such an option at this juncture, where thinking of raising funds through an IPO is confined to wild dreams, would certainly bring cheers to market and also would open the flood gates of boundless opportunities for the practising fraternities. A national level discussion on this subject would enable SEBI and other authorities to proceed further on these lines. □