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Sebi may make it mandatory for firms to buy back 50% of offer from investors

Reena Zachariah & Arun Kumar, ET Bureau Jun 21, 2013, 04.00AM IST

MUMBAI/NEW DELHI: Capital market regulator Sebi is set to overhaul the way companies buy back securities from investors through the stock market. The regulator is likely to make it mandatory for companies to buy back at least 50% of the proposed offer and if a firm fails to do so, it may have to forfeit 2.5% of the money earmarked for the buyback.

The regulator's board, which will meet on June 25, is expected to discuss the proposed rules, two people close to the issue said. An internal analysis by the regulator showed that some companies failed to buy a single share despite the buyback offer being open for an entire year. It had also observed that companies placed buy orders at their discretion.

Offer Within Six Months

The analysis showed that cos didn't place orders on regular basis. The orders were also placed at a price away from the market price. In order to ensure that only serious companies launch the buyback programme, Sebi is likely to make it compulsory for companies to put 25% of the total proposed amount for buyback in an escrow account and to complete their buyback offer in six months as against the existing one-year period.

However, there may be exceptions if the volume weighted average market price during the buyback period is higher than the buyback price and if there are inadequate sell orders despite the buy orders placed by the company. Investment bankers said the move would be helpful for investors as it would dissuade many companies who announce buybacks for public posturing.

"These measures are a right step towards plugging some of the loopholes that were prone to misuse. It would discourage companies that are not serious about implementing buybacks and were possibly making frivolous announcements without a real intention of undertaking a buyback," said Mehul Savla, director, Ripple-Wave Equity Advisors.

"Past experience has taught valuable lessons and most market participants today understand the nuances of a buyback through the stock market route and do not get swayed by the announcements of a buyback (especially at an optically high price) as shareholders may not necessarily get an exit at that price," he said.

Companies doing buyback programs may also not be allowed to raise fresh capital for one year. At present, companies are barred for six months from doing any fresh issue of shares from the date of buyback except by way of bonus, conversion of warrants, preference shares, debentures and stock option schemes.

Currently, buyback of shares can be done through two methods -- from the open market and through tender offers. Last year, the regulator changed the rules on tender offers and now its attempt is to revamp the stock market route as over 95% of share buybacks happen through market purchases.

The Sebi board will also discuss amendments to Alternative Investment Funds (AIF) rules to create a sub-category under venture capital called angel funds. These funds will be allowed to invest in unlisted companies that are not older than 3 years and whose turnover does not exceed Rs 25 crore. These investee companies should not be promoted or related to an industrial group whose turnover is in excess of Rs 300 crore, one of the persons quoted above said.

Investment by these funds should between Rs 50 lakh and Rs 5 crore and will have a lock-in for 3 years. Besides, no scheme of an angel fund should have more than 49 investors.

Although AIF regulations require minimum investment of Rs 1 crore by an investor, this is likely to be reduced to Rs 25 lakh for angel investment. The other proposals that are also likely to feature for discussions are on allowing small and medium enterprises (SME) and start-up companies on the SME platform without making an initial public offer.

In order to ring-fence the SME market only for the informed investors, the regulator is also proposing to increase minimum application size to Rs 10 lakh as against the current norms of maximum application amount of Rs 2 lakh for retail investors. The regulator also plans to allow MF distributors to become members of stock exchanges.