VEDANTA: DELISTING REGULATIONS NEED A RE-LOOK?

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VEDANTA DELISTING FAILURE

Delisting process which was kicked in by promoters of Vedanta in May 2020, finally came as cropper. The proposal could not sail through as Reverse Book Building ('RBB') could not get requisite number of bids in order to attain 90% equity threshold to discover a price which is must for a successful delisting. The entire delisting process has been a matter of intense debate since its initiation. Although the delisting has failed and promoters have withdrawn the offer, the entire episode has thrown various points for discussion. Some of the points are mentioned below which merit attention:

Floor Price, Book Value, Institutional Investors, Unconfirmed Bids and technical glitches:

- **SES in its various reports had stated that offer price given by the promoters, was unfair and Opportunistic.** Investors must ignore the same.
- **Many reports had suggested likely delisting price, based on funds mobilized by promotors and that became a sort of bench mark price for delisting. This was quite surprising, as all these reports forgot all valuation theories and parameters and funds availability became main factor.**
- **Unexpectedly, contrary to the public perception that Institutional Investors may succumb to a powerful high flying promoter, rather these Big Investors rose to the occasion** and proved all such analysts wrong & were not swayed by all the negative news floating around, or the Corporate pressure, if there was any. Thanks to these Investors, had the process been successful, discovered price would have been at ₹ 320, slightly higher than the top of valuation range of ₹ 236 – ₹ 310 suggested by SES.
- **Market did not pay any heed to the Offered price** (₹ 87.50) of the Promoters. It was also undeterred by write off gimmick which presented a **depressed Book value** (₹ 89.38).
- **'Unconfirmed Bids' proved to be a spoil sport. Had those bids got confirmed, the RBB would have discovered a price.** There is lack of clarity as to who were these bidders and why these bids (12.32 Crores shares) remained unconfirmed despite an opportunity to get a decent exit price.
- Had these bids been confirmed, **discovered price probably would have been around ₹ 320/-,** which is more than 350% of the Floor Price and Consolidated book value.
- Whether the Promoters would have accepted the price or not is a different question. But one thing is for sure, that the **market has clearly made the Promoters realize that shareholders cannot be taken for a ride. The Board must be feeling embarrassed as they certified offer at floor price to be in the interest of investors and supported** an opportunistic offer of ₹ 87.50/share from promoters.
- A question must be asked to board members as to why there is such a wide gap between what board felt to be in interest of shareholders and what shareholders themselves perceived to be in their interest. To find what is the fair price and whether that is in interest of shareholders, the Board could have asked a simple question, is the promoter willing to sell their equity at this price? This question rather being asked by SES, should have been asked by the Board, especially independent directors from promoters who proposed the Floor price.
- **42 lacs equity shares were tendered at a bid price of ₹ 90 or below**, when the trading price was above ₹ 110. Why would someone tender at around 20% discount if he can sell in market and realize cash immediately? To SES, this either indicates an attempt to send negative signals (which discerning investors ignored) or highlights the state of investor education.
- Since, the bidding process has failed, **can the Promoters again request another process for RBB**. What does the SEBI Delisting Regulation provide on this?
- SES would reiterate the need for SEBI to re-look at certain provision relating to the delisting Regulations to plug gaps.

Recap of Delisting Analysis

This would be the 5th Report of SES on the delisting topic concerning Vedanta. Previous 4 Reports can be accessed in the following manner:

S. No.	Particulars	Brief Content	Weblink to access the Report
1	Research Report dated 13th May 2020	Initial evaluation of the proposal of VRL to delisting Vedanta at an indicative price of ₹ 87.50/- per share	Click here
2	Proxy Advisory (PA) Report dated 5th June 2020	Detailed analysis of the Delisting proposal including an in-depth valuation undertaken on various parameters	Click here
3	Research Report dated 28th Sept 2020	Vedanta failing to pass on ₹ 12.18/- dividend to its shareholders, that is received from Hindustan Zinc Ltd (HZL)	Click here
4	Research Report dated 3rd Oct, 2020	Vedanta Delisting - Investors must bid without the fear of missing out. Value in share estimated at ₹ 256-310.	Click here

This Report intends to throw some light on various aspects of the Delisting process that need attention of the Regulator, so that we have a much more robust process in place.

TIME TO PLUG CERTAIN GAPS

1. Mystery of Unconfirmed Bids

There were close to 12.32 crores shares that were categorised as 'Unconfirmed Bids'. These bids were the boundary line in determining whether the price discovery process becoming successful or not. Since, these remained unconfirmed till the closure of the bidding period, the 90% threshold could not be achieved. Therefore, the price discovery mechanism failed and so did the delisting process.

There is lack of clarity around these unconfirmed bids. The questions that arise in the matter are:

- What are unconfirmed bids?
- Should such unconfirmed bids even be allowed?
- Who were these bidders?
- Why did their bids remain unconfirmed?

Going by the terminology, it appears these bids were placed, subject to some confirmation. Although, there is no mention of such bids in the Delisting Regulations.

SES is of the opinion SEBI must mandate that all the bids that are placed, must be confirmed by the shareholders before the last date of the bidding period and define what is meant by such bids. Otherwise there will be lot of confusion created over the fate of the price discovery as happened in case of Vedanta. SEBI must take care of this issue so that such issues could be avoided in future.

In Vedanta's case it is surprising that these bids remain unconfirmed even after lapse of considerable time. Such non-confirmation leads to a question, whether these bids were in effect real and backed by shares or these were hoax bids to give a false sense that 90% level is achieved if these bids are included? In fact, SEBI must call for data and find out who placed these bids and why they remain unconfirmed?

2. Time that Board members play a non-partisan role

Regulation 8(1B) of the SEBI Delisting Regulations requires the Board of Directors to certify that the delisting is in the interest of the shareholders. Invariably in all cases, the Board merely provides a statement that it certifies that the Delisting is in the interest of the shareholders, without in any manner justifying it.

The Board is the best judge of the performance and the inherent value of the business of the Company, therefore, such a vague statement is of no use to the shareholders, unless supplemented by explanation to justify as to why it considers delisting to be in the interest of the shareholders, or *vice versa*, as the case may be.

Guidance could be drawn from SEBI Takeover Code, where a committee of Independent Directors is formed to evaluate the takeover proposal and provide recommendation to public shareholders. Although, in case of Takeover the price is already available with the Committee, unlike the case of delisting proposal. Therefore, the Committee of IDs could comment on the floor price so determined and also the indicative price, if any, offered by the Promoters. Such a guidance of the Board or Committee of IDs shall help the public shareholders in taking a well guided and informed decision.

3. Voting pattern of Board members on delisting proposal

The role of the entire Board, especially the Independent directors is very critical in matters relating to Corporate Actions such as Delisting, Mergers & Amalgamations, etc. It may be noted that Rule 6(3)(iv) of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 mandates the following disclosure to be made in the Notice seeking shareholders' approval:

> ***6. Notice of meeting***
>
> *(3) The notice of the meeting to the creditors and members shall be accompanied by a copy of the scheme of compromise or arrangement, if such details are not already included in the said scheme: -*
>
> *(iv) the date of the Board meeting at which the scheme was approved by the Board of directors including* ***the name of the directors who voted in favour of the resolution, who voted against the resolution and who did not vote/ participate on such resolution****;*

If such disclosure is mandatory in case of scheme of Arrangement, where in most of the cases shareholders continue to remain part of business and approval is through judicial process, why such disclosure should not be mandated in case of delisting as well by SEBI regulations?

This would enable the shareholders to understand the stand taken by the Independent Directors in the delisting proposal.

4. Two-way offer price in delisting.

Present law gives a choice to promoter to make a delisting offer and right to refuse a discovered price without assigning any reason. As there is no risk in offering a price which is far below intrinsic or fair price, there will always be such offers, which would want to short change investors. SES is of the view that the law must be amended to ensure that only serious and fair offers are made. The law can mandate that:

- an acquirer while giving a CALL price must also give a PUT price, meaning that while indicating a floor price, there must be a requirement that acquirer must also declare at what price he would be a seller; Or
- law must make a provision that after acquirer declares a floor price, any other person can declare his willingness to buy promoters shares at 10% above declared floor price and offer the same price to public shareholders. This way law can ensure that only serious delisting bids will be made & fair price will be offered.
- For all non-serious offers, it is the shareholder who pays the cost of exercise as also suffers forsaking liquidity for about a fortnight. All such costs must be recovered in cases where offer is made below book value in case offer fails upon rejection by acquirer.
- Further a provision can be made that if promoters reject a discovered price, any third party can offer to purchase all tendered shares at discovered price with a commitment to buy remaining shares from other public shareholders. This would make delisting process fair with chances of success increasing.

This way only serious acquirer would dare to propose delisting price.

5. Promoter to accept shares at their own offered price

In Delisting proposal, the acquirer sometimes provide an indicative offer price at which they are willing to accept the shares from the public shareholders. This indicative offer price has no legal substance as price is determined through the book building process.

While, Regulation 16 give the acquirer authority to reject the RBB price, however, there is no provision in the Delisting Regulation mandating the acquirer to accept his own indicating offer. The Delisting Regulation must cover within its ambit such indicative offer price made by the Promoter, and must explicitly mandate them to accept the shares at the price indicated by them.

6. Consolidated Book Value for considering Counter Offer price.

Regulation 16 gives power to the acquirer to make a counter offer in case he rejects the RBB price. Such counter offer price shall not be less than the book value of the Company. However, the law is silent as to whether the book value must be computed on a standalone or consolidated basis.

The law must categorically state that such book value must be computed on a consolidated basis, after subtracting minority interest. The entire business that is attributable to the controlling shareholders must considered for the purpose of computing the book value.

While, the Regulation is presently silent on the issue, it would be desirable if the Regulation specifically mandates the same. Further, opportunistic write offs must be excluded/ not permitted.

7. Sudden write offs to reduce the book value of the Company

Since, the book value plays an important role in price determination in case of counter offer, there must be some regulation or monitoring over the provisioning / write offs / impairment recognition in the balance sheet which may lead to reduction of the book value.

While, there may be genuine need for the above write offs, however, as appeared in case of Vedanta, such write offs may solely aimed at reducing the book value with a view to reduce the counter offer price. In such cases, any abnormal write offs must be required to be certified by an independent Chartered Accountant, Registered Valuer or an appropriate expert.

This would ensure that the books are not manipulated to suit the interest of a particular shareholder/ group of shareholder(s).

8. Ten days to return equity shares?

Regulation 19 of the SEBI Delisting Regulations require that where the offer fails, the equity shares shall be returned or released within ten working days from the end of the bidding period. Time period of 10 days was understood in the old days when securities were in physical form and the process involved many steps. However, today baring few exceptions, all shares are held in dematerialised form. For instance, more than 99% of public shares of Vedanta are held in demat form.

Therefore, SEBI must re-look its 10 days deadline. SES is of the opinion that equity shares held in demat form must be returned the same day, when it is announced that the delisting has failed. This can be done since, shares are held in electronic mode and does not involve any physical transfer of goods or execution of any documents.

9. Can another attempt to delist be made?

It may be noted that 93% of the public shareholders (who voted) had given their in-principle consent for the Company to delist from Stock Exchange, subject to price discovery. Since, the shares tendered during the Reverse Book Building Process could not meet the requisite threshold of 90%, therefore, process of price discovery has failed. Now, the question is that whether the Promoters could try another attempt to initiate second round of price discovery?

While, the law is silent on the above issue, it appears that a fresh round of price discovery must be preceded by a fresh shareholders' approval. Another important question is that should there is any gap between 2 price discovery processes?

If Yes, then, what should be an ideal gap? Regulations are silent on this aspect.

10. State of Investor awareness / education

The Share price of Vedanta had a low market price of around ₹ 110 during the tender period. While, scrolling through the bidding disclosure available on the BSE website, SES came across the fact that certain bids amounting to 42 lacs equity shares had been tendered at a price of ₹ 90 or less. This pegs a question that why would a sane investor tender his / her shareholding at such significant discount?

Was it an error of judgement or lack of proper education?

Or it was a ploy to project a negative sentiment to everyone?

Unless the matter is investigated by the authorities, it is hard to justify such an unrealistic bid price.

11. Time Frame

At present, Regulations provide one-year time frame post shareholders' approval in which Promotors must make a final application to stock exchange. SES is of view that a reasonable time must be given. In this particular case, the Promoters took their own time and launched offer after almost 4 months from shareholders' approval. A pending delisting proposal creates an uncertain trading environment and continuing uncertainty for almost 5 months, vitiates free price discovery process. Therefore, as per SES, time period of one-year is too long. SEBI must prescribe time frame for all activities as freedom to decide within a year causes uncertainty.

CONCLUSION

Many other Companies viz, Adani Power, Hexaware Tech and Allcargo Logistics are also queued up for delisting from bourses.

Although, the Delisting attempt to delist Vedanta from bourses has failed, it is high time that SEBI addresses the concern raised by SES in this report. A robust delisting mechanism would enable it to not only protect the larger interest of various constituents of the capital market, but will also make it robust and fool-proof.

SES urges / expects SEBI to consider and fix the issues raised in this Report by making appropriate amendments in this regard.

RESEARCH ANALYST: VARUN KRISHNAN | JN GUPTA

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