Listing Reforms

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Listing means formal admission of a security into a public trading system, usually a stock exchange, often evidenced by a listing agreement between the issuer of the security and the stock exchange. It provides liquidity to investors without compromising the need of the issuer of security for capital and ensures effective monitoring of conduct of issuer and of trading of securities in the interest of investors. The issuer wishing to have trading privileges for its securities on a stock exchange satisfies listing requirements prescribed in the relevant statutes and in the listing regulations of the concerned stock exchange. It also agrees to pay the listing fees and comply with listing requirements on a continuous basis. The listing requirements usually include numerical criteria (issue capital, size of public offer), qualitative standards (corporate governance), and disclosure and reporting requirements.

Regulatory Framework

Listing of securities on Indian stock exchanges is essentially governed by the provisions in the Companies Act, 1956, the Securities Contracts (Regulation) Act, 1956 (SC(R)A), the Securities Contracts (Regulation) Rules (SC(R)R), 1957, rules, bye-laws and regulations of the concerned stock exchange, the listing agreement entered into by the issuer and the stock exchange and the circulars / guidelines issued by Central Government and SEBI.

The Companies Act, 1956 requires a company intending to issue securities to public to seek permission for dealing with its securities on one or more recognised stock exchanges. The prospectus should state the names of the stock exchanges where application for listing has been made and any allotment of securities shall be void if permission for listing is not granted by all the stock exchanges before expiry of 10 weeks from the closure of the issue. If application for listing is not made or if permission is not granted, the company shall repay all the moneys received from the applicants within 8 days.

In terms of the SC(R)A, SEBI grants recognition to a stock exchange after being satisfied that the bye-laws of a stock exchange are in conformity with the prescribed conditions to ensure fair dealing and to protect investors. A recognised stock exchange, subject to previous approval of SEBI, makes byelaws for the regulation and control of contracts. The Exchanges is empowered to make bye-laws which may provide for the listing of securities, the inclusion of any security for the purpose of dealings and suspension or withdrawal of any such securities and the suspension / prohibition of trading in specified securities. Where securities are listed on the application of any person in any recognised stock exchange, such person is under obligation to comply with the conditions of listing agreement with that stock exchange. On failure to comply with the conditions of listing, he shall be punishable with a fine up to Rs. 1, 000. A company can prefer an appeal to the Securities Appellate Tribunal (SAT) against refusal of a stock exchange to list its securities.

The SC(R)R prescribes requirements with respect to the listing of securities on a recognised stock exchange and empowers SEBI to waive or relax the strict enforcement of any or all of them.

A company seeking listing has to satisfy the stock exchange that at least 25% of the securities is offered to public for subscription. This requirement of offering 25% of the securities to public has been relaxed by SEBI in respect of the companies in the information technology, media (including advertisement), entertainment and telecommunication sectors, subject to the condition that at least 10% of the capital issued, comprising a minimum of 20 lakh securities, are offered to the public, and the size of the net offer to the public (i.e. the offer price multiplied by the number of securities offered to the public, excluding reservations, firm allotment and promoters' contribution) is not less than Rs. 50 crore.

The SC(R)R also confers a right on a recognised stock exchange to suspend or withdraw admission to dealings in the securities either for a breach of or non-compliance with any of the conditions of admission to dealings or for any other reason. Where a recognised

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stock exchange has withdrawn admission to dealings in any security or where suspension of admission to dealings has continued for a period exceeding three months, the company concerned can prefer an appeal to SAT, which may vary or set-aside the decision of the stock exchange.

The bye-laws of the Exchange authorise it to permit dealings in securities, listed or permitted to trade. It can permit dealings in any securities admitted to dealings on any other Exchange. It can refuse admission to dealings on the Exchange to the securities of an issuer, unless it complies with listing conditions and requirements prescribed in their bye-laws and regulations or such other conditions or requirements as it may prescribe. Under the bye-laws, the Exchange may suspend the admission to dealings on the Exchange granted to any security. The bye-laws also authorise it to withdraw the admission to dealings on the Exchange granted to securities either for breach of or non-compliance with any of the listing conditions or requirements.

The listing agreement contains a provision requiring the issuer to irrevocably agree that unless the Exchange agrees otherwise, the issuer will not, without the previous permission in writing of the SEBI, withdraw its adherence to the agreement for listing. It also requires an issuer to agree that any of its securities listed on the Exchange shall remain on the list entirely at the pleasure of the Exchange which has right to suspend or remove from the list the said securities at any time and for any reason which the Exchange considers proper in its absolute discretion. As a precondition for continuous listing, an issuer undertakes to forthwith comply with such future conditions as may be prescribed by the Exchange. Central Government / SEBI advises the Exchange to amend listing agreement and seek confirmation from it that the amendments have been effected. Central Government, SEBI and the Exchange keep on adding additional requirements to be complied with by the issuers.

A government circular requires that the companies wishing to list their securities must get listing on the regional (an exchange is considered regional for the state / Union Territory where it is located) stock exchange nearest to their registered office. If they so wish, they can seek listing on other exchanges also. All the exchanges where application has been made for listing must dispose off applications within the time specified in the Companies Act.

A SEBI circular requires the basic norms for listing of securities on the stock exchanges to be uniform for all the exchanges who may prescribe additional norms over and above the minimum norms. These norms are part of the bye-laws of the stock exchanges. SEBI has been issuing guidelines / circulars prescribing certain norms to be included in the listing agreement and to be complied with by the companies. For example, a SEBI circular requires that there will be at least 5 shareholders for every Rs. 1 lakh of net capital offer made to the public.

The SC(R)R, the bye-laws, the listing agreement prescribe a number of requirements to be continuously complied with by the issuers for continued listing. Such compliance is monitored by the Exchange. Failure to comply with the requirements invites suspension of trading of the security for a specified period, or withdrawal / delisting, in addition to penalty prescribed in the SC(R)A. SEBI circular permits voluntary delisting of securities from non-regional stock exchanges after providing an exit opportunity to holders of securities in the region where the concerned Exchange is located. An Exchange can, however, delist the securities compulsorily following a very stringent procedure.

Working of the Framework

Under the current dispensation, while it is mandatory to list a security on a regional exchange, it can be listed on any number of exchanges. The issuer has option to list its securities on any one or more of the exchanges. A security listed on one exchange can be permitted for trading on another exchange. Unless the regional exchange agrees to list a security, it can not be listed on any other exchange. The issue fails if the regional exchange refuses listing. The issue also fails if any of the exchanges, to which application for listing has been made, refuses to list the security. Further, a security can be delisted from all exchanges except the regional exchange. This arrangement generates unhealthy competition and wastage of resources in terms of duplication of efforts. There is a competition among the issuers to list securities on as many as exchanges as possible to attract investors from all over the country and waste resources to comply with the listing requirements of a number of exchanges simultaneously. Similarly there is a competition among the exchanges to attract as many issuers as possible at times leading to dilution of listing standards particularly when listing constitutes a major source of income for many of them.

They also waste resources as a number of them simultaneously monitor compliance with listing requirements which are by and large uniform across exchanges.

A security not found suitable for listing on an exchange gets listed on a different exchange, as they follow different criteria for listing a security. It may be noted that though the criteria for listing of securities differ across exchanges, the compliance requirements are essentially same. As a result, a prospective issuer informally gets a feedback from an exchange if the latter would consider listing of his security favourably. If he does not get an encouraging response, he tries his luck with other lenient exchanges. This precisely explains relatively high incidence of vanishing companies on lenient exchanges. This creates an anomalous situation that a security, which is not suitable for investors in one locality, is suitable for investors in another locality. A security should either be suitable for listing on all exchanges or not suitable at all for listing on any exchange, that is, it should be suitable for all investors or not for any. Similarly, securities can be delisted from all exchanges except the regional exchange. This means that the investors living in the locality of the regional exchange are closer than those living in other locations to the hearts of regulators are.

For all practical purposes, listing agreement is a one sided agreement requiring the issuer to agree to all the conditions prescribed at the time of signing the agreement or to be prescribed subsequently. The agreement is also amended unilaterally. The issuer has absolutely no choice in the matter as none of the terms is negotiable. The issuer is deemed to have agreed to comply with anything that may be prescribed at any time. Even the stock exchange does not have any freedom to vary any of the terms of the agreement. Why should we call it an agreement if both the parties to it have to blindly sign it? Why there should be separate agreements for each security if it is the same agreement? Why should an issuer sign the same agreement with a number of exchanges? It is just a waste of time. Since the terms are uniform across securities and exchanges, the issuers of securities can be asked to comply with a standard set of requirements specified in the SC(R)R. If a security is available for trading on an Exchange, the Exchange and the issuer can be deemed to have entered into a listing agreement.

Every now and then the listing agreement is amended to give effect to some policy decision of the regulators. Listing agreement is being increasingly used as the instrumentality of change, particularly as a means to improve corporate governance. The substance of the SEBI code on corporate governance has been incorporated as clause 49 of the listing agreement. One wonders if the listing agreement is the only means available for bringing about discipline in corporate sector, particularly when non-compliance with listing agreement can at best invite a penalty up to Rs. 1, 000. Trading of securities can be suspended or withdrawn, but this becomes a penalty on the investor. The stock exchanges are at loss to enforce the listing agreement. When there is no effective means to ensure compliance with listing agreement, there is no point in expecting a lot from it. It is no argument that the market would punish the issuers, as many of them happen to be one-timers or have no intention of accessing the market again. If investors are to be retained in the market, listing agreements have to be enforced.

An obnoxious practice of conditional listing that has developed in the market hurts investors. As the stock exchange is required to take a decision on the request for listing of a security within 70 days of the closing of the issue (otherwise the issue fails), at times a tentative decision is taken. The stock exchange accords conditional listing and allows trading only on fulfillment of the conditions. If the conditions are not fulfilled, the permission for trading is never granted. In such cases, the issuer gets subscription money and the Exchange gets listing fee, but investors hold securities but can not trade in them. They suffer silently as they fail to distinguish between listing and trading. Neither the SC(R)A nor the bye-laws made thereunder empower an exchange to grant conditional listing. Compliance of the conditions is condition precedent to listing, and not a post-listing requirement. In a recent order, the SAT has condemned (Goldline Financial Services Limited Vs. Hyderabad Stock Exchange) such conditional permission which endangers the interests of investors. Since such conditional permission negates the protection available to subscribers, it has advised SEBI to probe into the matter and take proper corrective and punitive measures to protect the interests of the investors.

The SC(R)R prescribes that at least 25% of securities must be offered to public in order to be eligible for listing. However, companies in select sector can offer less than 25% to public. The requirement is that at least 25% of securities must be offered to, not subscribed by public. There is no requirement that public holding must be at least 25% as long as the security remains listed. This results at time in very little floating stock. If the objective is to make a certain number of securities available in the market so as to avoid any possible manipulation of prices, there is a need to prescribe requirements of initial listing as well as continued listing, irrespective of the sector to which a company belongs.

Centralised Listing Agency

In order to take care of such anomalies, the SAT has recently suggested (Lunkad Media and Entertainment Limited Vs. The Stock Exchange, Mumbai) government and SEBI to consider the feasibility of providing a centralised mechanism to grant listing of securities on the stock exchanges. It felt that some sort of uniformity in deciding application for listing by exchanges would be in the interest of investors. It observed: "It does not stand to reason that a public issue found unacceptable by one exchange for the reason that the issuer company's credibility is doubtful, is acceptable to another exchange, though both the exchanges are supposed to be concerned about the interests of the investors. Investor protection measures should not be confined to territorial jurisdiction of exchanges. It should be at national level. Decision by a centralised set up may perhaps help to provide transparency and also help to maintain consistency and uniformity in the field of listing."

A task force set up by Department of Company Affairs under the Chairmanship of Mr. S. Rajgopalan to suggest an effective action plan to operationalise the concept of corporate excellence and to improve India's global competitiveness and development of corporate culture has recommended a centralised listing agency. As listing signals that the issue has been properly supervised, the unwary investors take it as some kind of qualitative rating of the company, despite disclaimers to the contrary. This therefore requires tough standards for listing and strict compliance through a centralised National Listing Authority. This would remove dependence on the less active stock exchanges for whom listing fee is a principal source of income.

Similar sentiments are being echoed by professionals. In a recent article, Dr. R. H. Patil (Economic & Political Weekly, November 18-24, 2000) has nicely articulated the need for central listing agency. Most of the exchanges are "Association of Persons" which was considered beneficial in terms tax benefits and matters of compliance. They are having re-look at the way they conduct business and are gearing up to demutualise themselves by converting themselves into a public limited company. They will also be accessing securities market to finance their ever expanding trading network and would be interested to list their securities. This would create an anomalous situation where a stock exchange would admit its own securities for trading. A satisfactory solution may be to vest the listing powers with a body separate from stock exchanges. Further, listing casts a number of these obligations on issuers and on exchanges. Many of the exchanges are too weak organisationally to monitor compliance of obligations. Many of the issuers find it difficult to comply with the requirements separately for different exchanges. In view of this, it is desirable that there is only one central agency which considers all requests for listing and grants listing if it finds a security suitable for investors across the country. A security granted listing by the agency would be available for trading on all exchanges who will not waste resources in terms of duplication of efforts on listing and monitoring compliance. The security should also be monitored, and suspended and withdrawn from trading centrally by the listing agency. The investors and market participants would get all the company related information, which are mandatorily required to be filed by companies with stock exchanges or any other agency, at one central location preferably a web site.

Most of the compliance under the listing agreement requires disclosure from the company. SEBI has recently advised amendment to listing agreement requiring the companies and the stock exchanges to post certain information on their web sites. The exchanges have also been advised that when any information regarding material event is received from a company for which the stock exchange is the regional stock exchange, the same shall be disseminated to all the exchanges where the securities of the company are listed or traded without prejudice to the obligation of the company to inform all the stock exchanges where the securities of the company are traded. This casts onerous responsibilities both on the exchanges and companies and a lot of duplication. If the objective is to allow the investor make an informed decision by making details of the companies available to them, it would be better to display all these at one central place. The details can be filed, updated and retrieved electronically and instantaneously. SEBI is considering such an integrated source of company information on lines similar to that of Electronic Data Gathering, Analysis and Retrieval (EDGAR) system in the USA.

Listing on Regional Exchanges

The stock exchanges are the exclusive centres for trading of securities. The regulatory framework favours them heavily by almost banning trading of securities outside exchanges. Until recently stock exchanges enjoyed monopoly in the respective cities where they were located. Monopoly of the exchanges within their allocated area, regional aspirations of the people and mandatory listing on the regional stock exchange resulted in multiplicity of exchanges. There are 24 exchanges in the country recognised over a period of time to enable investors across the length and breadth of the country to access the market. SEBI recently ended the rule that precluded competition among regional exchanges. Now all regional exchanges can freely expand their operations to any other location of their choice. Many of them have expanded trading operations to different parts of the country. The two newly set up exchanges (OTCEI and NSEIL) have been mandated since their inception to have nation wide trading. The trading platforms of many exchanges are now accessible from a location. Further, with extensive use of technology, the trading platforms of a few exchanges are also accessible from any where through the Internet and mobile devices. This has made a huge difference in a geographically vast country like India and assuaged the grouse of small investors in far-flung locations who do not have proper access to a stock-broker and the market. It has significantly expanded the reach of the exchange to the homes of ordinary investors. In such changed environment, the need to provide opportunity to investors to invest in securities of local companies through listing on regional exchange may not be relevant. In any case, site of the registered office does not determine the investor base. Further, in the liberalised environment, a company should have liberty to list its securities on the exchanges of its choice.

Delisting

It is argued by investors that on the promise in the prospectus that a security would be listed on a stock exchange, they subscribe for the securities. Since their decision is irreversible, the promise in the prospectus should also be irreversible. This means that a security once listed should never be allowed to be delisted. That is why probably there is no explicit provision about listing in the statutes. However, circumstance changes which may require a review of the promise and delisting may be desirable. In such cases, securities should be delisted from all exchanges, including the regional exchange, provided that an equally efficacious exit is available for the investor.

Many listed companies do not comply, at times deliberately, with the conditions of listing. This normally invites the soft option of suspension of trading or delisting. In the past many securities have been delisted on filmsy grounds. Though there is a statutory obligation on the person, on whose application securities are listed on an Exchange to comply with the conditions of listing agreement, this has hardly been used to take such person to task if he has failed to do so.

Non-payment of listing fee has been a common cause for delisting of securities. Many companies find it burdensome particularly when the securities are rarely traded. Exchanges have temptation to bend rules to list a security as they can get listing fees. Why should exchanges charge and the companies pay a listing fee? The exchanges do not levy any such fee from permitted securities. The direct beneficiaries of listing are the investors. The volume of services rendered by an Exchange for a security depends on the its trading volume. It may be better if investors pay an insignificant charge to the Exchange for every trade they undertake in the security. The Exchange in turn should part with a part of this insignificant charge to the listing agency.

In addition to voluntary delisting and compulsory delisting by the issuing company and the concerned stock exchange respectively, the securities are also delisted by operation of law. For example extinction of securities by exchange or conversion into other securities as a result of any scheme of reorganisation or on liquidation. If a company is liquidated, the security disappears. What happens, if an exchange where securities are listed, disappears? Given the technological change, extinction of stock exchanges is not a remote possibility. This reinforces the argument that securities should be listed, but not listed on a particular stock exchange. A security once listed should be available for trading on any exchange.

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