UNRAVELLING SEBI'S CONSULTATION PAPER: CHANGING LANDSCAPE OF INDIA'S DEBT SECURITIES MARKET

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ABSTRACT

In a breakthrough development in India's financial market landscape, the Securities and Exchange Board of India ("SEBI") has released a consultation paper with the goal of promoting ease of doing business and reducing burden of compliances on corporate entities by proposing amendments to SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 ("LODR Regulations") and SEBI (Issue and Listing of Non-Convertible Securities) Regulations, 2021 (NCS Regulations). Besides this, the move has brought home, the idea of 'fast tract public issue' framework for debt securities so as to enhance public participation and promote overall market development. The Consultation Paper came into being based on the interim recommendations made by an Expert Committee tasked with improving transparency, easing business operations, and harmonizing regulations within the frameworks of the LODR Regulations and SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018 ("ICDR Regulations"). This essay attempts to explore the paper's background, deliberating on the chain of chronological developments, key features and proposals, resulting challenges & limitations while offering learning lessons from around the world for the development of India's debt securities market.

Introduction

The market for debt securities in India has been expanding over the years. Reserve Bank deputy governor, Rabi Sankar observed that "the concerted efforts by regulators and government have seen corporate bond outstanding has crossed Rs 40 lakh crore as of March 2022 from Rs 10.4 lakh crore in March 2012, while annual issuances rose to Rs 6 lakh crore from under Rs 4 lakh crore during this period. During the same period, the secondary market volume spiked from Rs 4.4 lakh crore to Rs 14 lakh crore."[1] The market is however faced with innumerable challenges and regulatory roadblocks including complex and onerous regulatory requirements, insufficient liquidity and transparency, high issuance and listing costs coupled with shrinking retail participation.[2]

Promoting a conducive business environment at this juncture, requires establishing a harmony between stringent regulations and minimizing needless administrative hassles. The corporate bond market in India is predominantly a private placement market with less than 2% participation from non-institutional investors.[3] The existing framework ushered by the publication of the "consultation paper on review of provisions of NCS Regulations and LODR regulations for ease of doing business and introduction of fast-track public issuance of debt securities" by SEBI, has been designed to promote public issuances in the corporate debt market and boost the participation of non-institutional investors.

This essay attempts to explore the paper's background, deliberating on the chain of chronological developments, key features and proposals, resulting challenges & limitations while offering learning lessons from around the world for the development of India's debt securities market.

Background Picture: A study of the timeline

The current revolutionary move can be traced back to a slew of events that preceded the

[1] ET Staff, 'Corporate bond outstanding soars four-fold to Rs 40 lakh crore in a decade' Economic Times (Mumbai, 24 August 2022).
[2] Nikita Singh & Aishana, 'Fast-Track Revolution: SEBI's Consultation Paper on Reforms in the Debt Securities Market' (IndiaCorpLaw, 17 January 2024) https://indiacorplaw.in/2024/01/fast-track-revolution-sebis-consultation-paper accessed 6 May 2024.
[3] Ajay Manglunia, 'Corporate bonds at an inflexion point: Time for some retail therapy' Economic Times (Mumbai, 26 Feb 2023).

development. SEBI's board meeting[4] on September 30th, 2022 to lower the face value of privately placed debt securities and the resulting amendment[5] to the circular which saw reduction in denomination for debt securities and non-convertible redeemable preference shares, is what marked the beginning of a gradual shift in the bond market. This was necessitated for bringing in inclusivity for non-institutional investors who were deterred by the then high face value for debt securities. The next big leap in this chain of developments was the setting up of a regulatory framework for online bond platforms[6], to foster efficient disclosure, transparency and better availability of redressal mechanisms.

This was followed by the Budget's (2023–24) aspirational focus on streamlining rules & regulations, cutting compliance costs, and creating a business-friendly environment, which nudged authorities to review existing frameworks with greater detail. With a specific focus on assessing provisions within the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (LODR Regulations) and the SEBI (Issue and Listing of Non-Convertible Securities) Regulations, 2021 (NCS Regulations), a specialized working group, the 'Corporate Bonds and Securitization Advisory Committee'[7] was established to propose measures enhancing the ease of doing business for listed debt issuers. The committee had observed that there is a need to govern the operations of online bond platforms to ensure enhanced regulatory oversight and governance.[8]

It is in this backdrop of steady and sustained growth in the securities market, that Securities and Exchange Board of India (SEBI) published a consultation paper[9] on December 9, 2023, suggesting regulatory reforms aimed at promoting expansion of the corporate bond market in India.

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[4] SEBI, SEBI Board Meeting, (Sep 30, 2022).
[5] SEBI, Reduction in denomination for debt securities and non-convertible redeemable preference shares (SEBI/HO/DDHS/P/CIR/2022/00144, 2022).
[6] SEBI, Registration and regulatory framework for Online Bond Platform Providers (SEBI/HO/DDHS/DDHS-RACPOD1/P/CIR/2022/154, 2022).
[7] SEBI, Corporate Bonds and Securitization Advisory Committee (CoBoSAC), https://www.sebi.gov.in/sebiweb/about/AboutAction.do?doMember=yes&committeesId=9.
[8] Shreya Dua, Anushri Uttarwar, Parth Tyagi, 'SEBI proposes regulatory framework for online bond platforms' (Khaitan and Co, 1 August 2022) https://www.khaitanco.com/thought-leaderships/SEBIs-proposed-regulatory-framework-for-online-bond-platforms accessed 7 May 2024.
[9] SEBI, Consultation paper on review of provisions of NCS Regulations and LODR Regulations for ease of doing business and introduction of fast-track public issuance of debt securities (9 December 2023).

Decoding Key Features: Debt Issuers and Retail Investors in Focus

Indian debt market is underperforming due to reduced participation from individual investors, burdensome laws and compliance requirements, and complex procedures for issuing and listing debt instruments. SEBI's move aims to expedite the process of issuing debt securities to the public and enhance the involvement of retail investors in the corporate bond market. In line with these objectives, SEBI plans to take the following measures for the issuers of debt and individual investors:

Leveraging interest of Debt Issuers:

SEBI has proposed to ease compliance requirements, simplify rules, and lower the costs associated with issuing and listing public debt securities. To achieve this, SEBI has put forward full-fledged mechanisms[10]; Engaging a merchant banker to conduct a thorough examination and provide information on privately placed Non-convertible Debentures (NCDs) and Non-convertible Redeemable preference Shares (NCRPs), considering that the securities may be issued at a value of Rs. 10,000; Inserting a QR code to provide a direct link to the audited financial statements from the last three years. This will save the need for repeating disclosures in the offer document and ensure that the offer document is filed in a timely manner.

The proposal further mentions streamlining timelines and disclosures as:

- Submissions of disclosures in compliance with Schedule 1 of SEBI (Issue and Listing of Non-Convertible Securities) Regulation 2021, are required to be made till the most recent quarter.

- The record date[11] to be standardized to 15 days before the payment of interest or redemption. This will prevent inconsistencies and promote uniformity in how record dates are handled in the market.

- Modification of the due diligence certificate under regulations 40 and 44 of SEBI (Issue and Listing of Non-Convertible Securities) Regulation 2021 aims to simplify and make

[10] SEBI, Consultation paper on review of provisions of NCS Regulations and LODR Regulations for ease of doing business and introduction of fast-track public issuance of debt securities (9 December 2023) 3-16.
[11] *Ibid. Record Date – it is date on which the investor must be the owner of the debt securities for corporate actions,* pg. 7-8.

more efficient the certification procedure.

- The consultation paper also suggests modification in regulation 52(8) of SEBI (Listing Obligations and Disclosure Requirement) Regulations 2023, a positive step towards reducing expenses. It now allows issuers to exercise discretion in publishing the conclusion of meetings in newspapers.

Fast-track public issue of debt securities:

Next in line is the most promising step of introducing a *fast-track public issue of debt securities* to make it easier for non-institutional investors to participate in the primary market. Introducing the Generic Information Document (GID) and Key Information Document (KID) were allied changes that were brought in to streamline disclosure requirements and replace the previous practice of issuing multiple memorandums. While GID provides information and disclosure as specified in Schedule 1 of NCS Regulations 2021, which is to be submitted to the stock exchange, KID includes additional information that is not found in GID (Part A), as well as specific details about the securities being offered. One needs to prepare the GID - KID offer document within a timeline of 2-3 weeks.

Additionally, the proposal mentions factors determining the eligibility of issuers to expedite the public issuance of their debt securities. This measure helps to establish the credibility of the issuer and the ratings given by the credit rating agency, as well as ensuring that there have been no regulatory actions taken against the issuer. It also seeks to streamline the process of seeking public comments on draft offers by reducing the time required to just two working days, instead of the current five working days. It also facilitates the issuers to utilize electronic methods for advertising the public issue, moving away from the traditional practice of publishing in newspapers.

Furthermore, the paper proposes changes to avoid delays in issuances and listing, including but not limited to removing the minimum subscription requirement for entities in the financial sector to ensure consistent funding for their operations, setting the time frame for fast-track public issue of debt securities to range from a minimum of 1 working day to a maximum of 10 working days with the possibility of an extension, prescribing the retention limit[12] at a maximum of 5 times the base issue for both public issue and private placement which essentially aims to enhance flexibility in raising funds, and limiting the time for listing debt securities for public issue to 3 days from the date of closure (T+3).

Leveraging Interest of Retail Investors:

SEBI has put forward a set of proposed changes aimed at facilitating greater public involvement in debt securities[13], in furtherance of which, the ticket size has been reduced to Rs. 10,000 in order to make it more accessible for noninstitutional investors and encourage greater participation from online bond platforms. This is a win-win for investors as a reduction in ticket size makes it more conducive to the diversification of portfolio, thereby suggesting greater profits and mitigates risk.

It is recommended to lower the minimum face value of debt securities issued privately, specifically non-convertible debentures and non-convertible redeemable preference shares. The scheme is implemented for simple interest-bearing bonds ("vanilla bonds") with a straightforward structure, the inclination towards which can be witnessed particularly post-2008 economic crisis. United States of America, for instance, promoted the issuance of plan vanilla debt instruments, thereby raising disclosures and compliances for non-vanilla debt securities[14].

It also aims to ensure fair and balanced participation while managing risk hurdles. To achieve this, the proposal suggests appointing a merchant banker to conduct thorough due diligence for the issuance of non-convertible debentures and non-convertible redeemable preference shares. Additionally, it emphasizes the importance of disclosing relevant information in the private placement memorandum. This comes as a positive development that allows issuers to reach out to non-institutional investors and expand their businesses.

[12] Kwangbong lee, Bruce A. Palmer, Harold D, "An Analysis of Life Insurer Retention Limits" , [March 1992] Vol. 59, No. 1 The Journal of Risk and Insurance 57, *Retention is the amount of any insured loss to be borne by the primary company.*

[13] SEBI, Consultation paper on review of provisions of NCS Regulations and LODR Regulations for ease of doing business and introduction of fast-track public issuance of debt securities (9 December 2023) 3-4.

[14] Ansh Chaurasia, 'Retail Investors in the spotlight: SEBI's Consultation Paper on Bonds' NLIU Journal of Business Laws < https://cbcl.nliu.ac.in/capital-markets-and-securities-law/retail-investors-in-the-spotlight-sebis-consultation-paper-on-bonds/ > accessed on 9 May 2024.

Zooming In: Analysing the Challenges & Implications

Zooming in the outer bubble of benefits, reveals challenges in the resulting implementation that dig deeper. One of the most innate and inevitable one, stems from the low inclination of retail investors towards bonds, in general. This comes as a result of escalating competition from government supported alternative debt instruments targeted specifically at retail investors, such as Savings Bonds and National Savings Certificates.[15] These instruments frequently yield more effective returns than marketable securities like bonds, which do not enjoy the same tax benefits. For corporate entities seeking financing, the "cost of capital is reduced as the interest expenses on debt instruments are tax-deductible, making it a more attractive option than other forms of financing."[16]

Another implementational challenge emanates from the highly underdeveloped Indian corporate bonds market.[17] By expanding the base of issuers in the primary market and promoting more active bond trading, a well-established secondary market improves liquidity and strengthens the price discovery process. This becomes concerning as the illiquidity of this market admittedly hinders the participation retail investors.

The possibility of information asymmetry between issuers and investors, which results from the reduced disclosure and compliance obligations of the fast-track public issue, is yet another cause of concern. This may compromise investor decision-making if issuers disclose inadequate information as a result of this.[18] To tackle this, it is essential to protect investor interests and market integrity by implementing strict materiality requirements and disclosure standards, as well as strong monitoring and enforcement measures by SEBI and the stock exchange.

One of the many changes proposed in the consultation paper is with regard to the process for ranking companies using the average market capitalization of listed firms during the previous

[15] Shalin Ghosh, 'Smaller Ticket Sizes: Decoding SEBI's Corporate Bond Market Reform' (IndiaCorpLaw, 21 December 2023) https://indiacorplaw.in/2023/12/smaller-ticket-sizes-decoding-sebis-corporate-bond-market-reform.html accessed 28 April, 2024.
[16] ET Staff, 'India's thriving bond market: A comprehensive overview' Economic Times (Mumbai, 4 December 2023).
[17] Ajeet Kumar Maurya & Prof. Raj Kumar, 'Corporate Debt Market in India: An Overview' (2012) SSRN 1.
[18] Nikita Singh & Aishana, 'Fast-Track Revolution: SEBI's Consultation Paper on Reforms in the Debt Securities Market' (IndiaCorpLaw, 17 January 2024) https://indiacorplaw.in/2024/01/fast-track-revolution-sebis-consultation-paper-on-reforms-in-the-debt-securities-market accessed 25 April, 2024.

six months, from July 1 to December 31, rather than the market capitalization of entities as of March 31. This may significantly impact a company's rating where any incident or market trend particularly affects the company during this span of time.[19]

Additionally, the proposed relaxations raise concerns regarding risk of market manipulation and investor protection, whose impact remains to be seen.

Taking Lessons from Abroad

- **United Kingdom**

The United Kingdom has introduced a new opportunity for investors to participate in the primary bond market, therefore expanding their financial freedom. In one of the first moves, Winterflood Securities, a government-designated dealer for UK debt, recently enabled private investors to purchase government bonds directly in the primary market[20]. The loan securities, known as gilts[21], issued by the UK government, which until now were only accessible to a select set of investors authorized by the Debt Management Office, is now set to see new dawn of the day as the Financial Conduct Authority plans to enhance retail investment in the capital markets.

The expedition commenced in June 2023 with the publication of consultation paper 23/10, which proposed incentives for the issuance of non-equity instruments, despite the occurrence of a series of mini-bond scandals[22]. Subsequently, the Financial Conduct Authority released Engagement Paper 4, which established a regulatory framework that supports issuers and investors of non-equity instruments and facilitates global debt financing.

The engagement paper 4 intends to employ the measures to widen the corporate financing[23] by; extending the validity of the basic prospectus to 12 months. This means that there will no

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[19] Avantika, 'Decoding SEBI's Consultation Paper: Path to Easier Listings and Reduced Compliance' (NLU Delhi, 13 March 2024) https://www.cbflnludelhi.in/post/decoding-sebi-s-consultation-paper-path-to-easier-listings accessed 2 May 2024.
[20] Mary McDougall, 'UK opens up gilts to retail investors' Financial Times (London, 22 February 2024).
[21] *Ibid.*
[22] Frank Daly, 'Time to reopen the UK bond markets to retail investors?' (RW Blears LLP, 23 November 2023) https://blears.com/wp-content/uploads/2023/11/Time-to-re-open-the-UK-bond-markets-to-retail-investors-November-2023.pdf accessed 6 May 2024.
[23] Financial Conduct Authority, Engagement Paper 4 'Non equity securities' (May 2023) < https://www.fca.org.uk/publication/call-for-input/non-equity-securities-engagement-paper-4.pdf >accessed on 9 May 2024.

longer be a need to publish a supplementary prospectus. Additionally, a deeming clause will be included, which allows for future elements to be integrated into the prospectus when they are published; Modifying the existing practice of having different disclosure standards for lesser denomination securities, and implementing a unified standard for bond disclosure together with a limited number of limitations and regulations to safeguard the interests of investors.

The paper also enables international access to corporate financing for straightforward, standardized, unsecured corporate bonds issued by experienced UK-listed firms, accompanied by substantial information. It necessitates reviewing the existing regulations governing intricate debt instruments, securitized derivatives, and other structured financial products, as well as the disclosure obligations for the entities issuing, originating, or organizing these securities.

In what is being seen as a promising turning point, it proposes modifying the criteria for issuing non-equity securities in secondary markets, such as implementing a simplified prospectus that closely resembles a final term document utilized in the issuance program after the base prospectus has been made available. It also deals with enhancing the correlation between the prospectus and bond framework to align goals, transparency, and application of the bond proceeds, particularly in relation to green, social, or sustainability-labeled financial instruments. The FCA's objective is to create clear and detailed information on the projects that these bonds are intended to fund, the management of the funds, compliance with particular industry requirements (such as climate bonds), and the level of sustainability. The proposal is to introduce new listings on the professional securities market and accept admission papers as a prospectus. While existing companies will be allowed to continue their operations, this proposal does not allow any new firms to be added to the list of professional securities market.

Conclusively, the UK has implemented significant changes to its debt financing structure to encourage greater investor involvement, reduce costs for issuers, and streamline the due diligence.

- **United States of America**

The bond market in the United States, known as the fixed-income market, is one of the largest globally, accounting for 41% of the $122.6 trillion worth of outstanding securities worldwide[24]. It encompasses a diverse range of goods such as U.S. government bonds, Treasury bonds, Corporate Bonds, and more. The regulation of the bond market in the United States is overseen by the Securities Exchange Commission (SEC) in accordance with the US Securities Exchange Act of 1934, as well as the regulations set out by the Financial Industry Regulatory Authority (FINRA) and the Municipal Securities Rulemaking Board[25].

Among the several types of debt instruments, some notable examples are publicly traded U.S. Treasury bonds, US Agency bonds, and privately traded business bonds[26]. These debt securities, which are issued to the public, must comply with certain requirements[27] like; submission of annual, quarterly, and current reports for publicly issued debt instruments by the issuer; submission of a valid indenture in compliance with the US Trust Indenture Act of 1939, which outlines the terms of securities and is established between the issuer, guarantor, and trustee; submission of a registration statement, which includes a prospectus, to the Securities Exchange Commission for assessment, except for well-known seasoned issuers. Obtaining permission from FINRA is another need for a public offering. These prospectuses are publicly available on the SEC website. After the registration statement becomes effective, a term sheet is submitted to the SEC, specifying the offer price, interest rate, and other parameters[28]. The subsequent crucial action is to submit a conclusive prospectus encompassing price details.

The United States has implemented a comprehensive system of paperwork and disclosures, which requires several authorizations and involves the responsibilities of legal advisors, auditors, and underwriters. As a result, investing in debt securities in the United States is comparatively safer for the general public.

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[24] Securities Industry and Financial Markets Association, 'Understanding Fixed Income Markets in 2023' (9 May 2023) https://www.sifma.org/resources/research/understanding-fixed-income-markets-in-2023/ accessed 7 May 2024.

[25] Cleary Gottlieb Steen, 'Debt Capital Markets in the USA' (*Hamilton LLP*, 4 April 2019) https://www.lexology.com/library/detail.aspx?g=79f01516-cf6f-4fe6-a580-e0726a969497 accessed on 7 May 2024.

[26] Ralph S.J. Koijen and Motohiro Yogo, 'Understanding the Ownership Structure of Corporate Bonds' [January 2022] Working Paper No. 2022-17 Becker Friedman Institute <https://bfi.uchicago.edu/wp-content/uploads/2022/01/BFI_WP_2022-17.pdf> accessed on 7 May 2024 .

[27] Securities Industry and Financial Markets Association, 'Understanding Fixed Income Markets in 2023' (9 May 2023) https://www.sifma.org/resources/research/understanding-fixed-income-markets-in-2023/ accessed 7 May 2024.

[28] *Ibid.*

However, the worldwide crisis in 2008, which was initiated by the United States through sub-prime lending, is ingrained in our collective memory. This catastrophe serves as a reminder of the risks involved in investing in debt instruments[29] specified as: *Default Risk* which refers to the likelihood of failing to meet debt obligations; *Interest Risk* having potential for price fluctuations in bonds due to changes in interest rates; *Inflation Risk* having potential to mutate the income earned from bonds which may decrease if the overall price levels increase; *Liquidity risk* which refers to the possibility that the seller (investment) may encounter difficulty in locating a buyer. Nevertheless, these risks may be reduced by diversifying the investment portfolio, examining the prospectus, and acquiring knowledge about the financial state of enterprises through regular reports submitted by them, something which US seems to ace at.

Conclusion

The 'Consultation Paper' released by SEBI is indeed a noteworthy step towards addressing the problems plaguing the Indian corporate debt market. The move aims to increase investor involvement, accelerate fundraising, and enhance transparency and efficiency. The paper uncovers a strong commitment to enhancing disclosure standards and making business easier to conduct. Additionally, in order to improve retail investor participation and streamline public issuances in the debt market, SEBI has addressed several concerns by proposing necessary amendments to LODR and NCS Regulations.

However, a close inspection reveals potential vulnerabilities in the requirements for eligibility, disclosure channels, subscription durations, and minimum standards.[30] The drawbacks and hazards associated with the proposed amendments call for a cautious thought. Accelerating the issuing process could weaken due diligence requirements, raise the risk of defaults or insufficient disclosures, and jeopardize investor protection and market integrity. Furthermore, a sudden influx of debt securities could undermine market stability. By adhering to strict monitoring and ongoing assessment to reduce risks and preserve market resilience, SEBI must come up with a balanced strategy to counter these possible challenges.

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[29] SEC Office of Investor Education and Advocacy, ' What are corporate Bonds?' (SEC Pub. No. 149 (6/13) <https://www.sec.gov/files/ib_corporatebonds.pdf> accesses on 7 May 2024.

[30] Dhaval Bothra and Rajdeep Bhattacharjee, 'A Faster Track for Debt Financing: Examining India's Proposed Public Issuance Framework' (IndiaCorpLaw, 3 January 2024) https://indiacorplaw.in/2024/01/a-faster-track-for-debt-financing-examining-indias-proposed-public-issuance-framework.html accessed 9 May 2024.