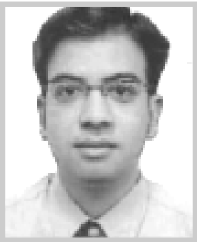

Fund Raising Abroad through Euro Issue

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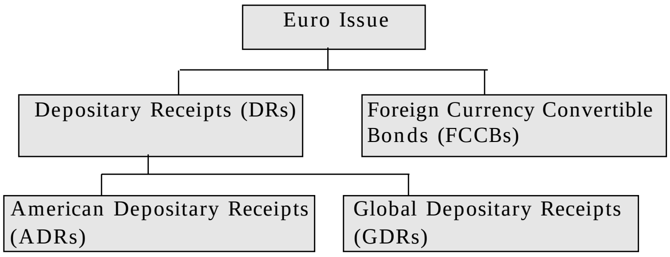
INTRODUCTION

The term 'Euro Issue' does not bear any specific meaning nor is it a legal term one. It denotes an issue of securities to be listed abroad (normally on a European Stock Exchange). It is a mode of raising funds by an Indian company from abroad in foreign currency.

Euro Issue may broadly be explained as under –



In terms of the definition provided under the Foreign Currency Convertible Bonds and Ordinary Shares (Through Depository Receipt Mechanism) Scheme, 1993 (the Scheme), "Global Depository Receipts means any instrument in the form of a Depository receipt or certificate (by whatever name it is called) created by the Overseas Depository Bank outside India and issued to non-resident investors against the issue of ordinary shares or Foreign Currency Convertible Bonds of issuing company."

Euro issue has been one of the important sources of fund raising for India Inc. Importance of Euro issues has increased in recent times as more and more companies are approaching overseas markets to tap the required funds. This article covers important statutory conditions relating to and working mechanism of Euro issues.

Although the nomenclature of DRs may vary, depending upon the target investors and applicable regulations, the basic features remain the same.

Foreign Currency Convertible Bond (FCCB), an equity-linked security, is a convertible bond that can be exchanged, at the option of the holder, for a specific number of shares of the issuer company.

In terms of the Scheme, "FCCBs" mean bonds issued in accordance with the FCCB scheme (1993) and subscribed by a non- resident in foreign currency and convertible into ordinary shares / depositary receipts of the issuing company in any manner, either in whole, or in part, on the basis of any equity related warrants attached to debt instruments.

BENEFITS

DRs have become very popular – both as a tool for accessing global capital markets as well as an investment vehicle. The main benefits of DRs to issuer companies as also to investors are summarised hereunder –

Why Do Investors Invest In DRs – Popularity of DRs as Investment Vehicle

- Convenience of holding foreign securities in their markets.
- Diversified Portfolio.
- Simplification of trading and settlements (DRs trade and settle just like US or Euro securities).
- No restrictions on dealing; DRs are recognised as domestic securities.
- Avoids currency risk of holding local shares

Why do Companies issue DRs – Popularity of DRs as tool for accessing global capital markets :

- Raise capital.
- Diversify share-holder base into extended geographies.
- Increase visibility and recognition in international markets.
- Increase the liquidity of underlying shares.
- Global image.
- Set up Employee Stock Option Plans (ESOPs) .
- Facilitate M&A activity by creating a desirable acquisition currency (if DRs listed abroad).

IMPORTANT STATUTORY CONDITIONS

Track Record

Since 2000, the track record condition is no longer operative for ADR / GDR issues.

However, a company seeking permission for raising foreign funds by Euro-issues having a consistent track record of good performance (financial or otherwise) for a period of 3 years will be allowed to issue FCCBs.

In view of the importance of the infrastructure projects, and the need to encourage equity financing of such projects, the 3 years track record requirement would be relaxed in case of companies

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seeking FCCB issues to finance investments in infrastructure industries such as power generation, tele-communication, petroleum exploration and refining, ports, airports and roads.

Eligibility and Pricing

In this regard, new norms brought into force by the MOF Notification dated August 31, 2005 would apply. One of the foremost conditions is simultaneous listing of shares of the issuer company on Indian bourses, if the shares are not already listed. Pricing norms as applicable in case of preferential allotment have been prescribed for Euro Issues as well.

Lock-in

No Lock-in period has been prescribed for DRs/FCCBs.

Listing & Trading

DRs/FCCBs issued may be listed on any of the Overseas Stock Exchanges, or Over the Counter Exchanges or through Book Entry Transfer Systems prevalent abroad and such receipts/ bonds may be purchased, possessed and freely transferable by a non-resident.

APPROVAL MECHANISM

DRs : Indian companies raising money through DRs are under the automatic route without requiring the prior approval of the Ministry of Finance, Department of Economic Affairs.

Private placement of DRs would also be eligible for the automatic approval provided the issue is lead managed by an investment banker registered with the US Securities and Exchange Commission, or under UK Financial Services Act, or the appropriate regulatory authority in Europe, Singapore or Japan.

In all cases of automatic approval, the mandatory approval requirement under FDI policy, approvals such as under the Companies Act, approvals for overseas investments/business acquisition (where DR proceeds are utilised for overseas investments) etc., if applicable, would need to be obtained by the company prior to the DR issues.

FCCBs : A person resident in India, being an Indian company or a body corporate created by an Act of Parliament :-

(i) may issue FCCBs not exceeding US$ 500 million to a person resident outside India in accordance with and subject to the conditions stipulated in Schedule I to the Foreign Exchange Management (Issue of Foreign Security) Regulations.

(ii) may issue FCCBs beyond US $ 500 million with the specific approval of the RBI.

DRs/FCCBs to be issued will have to conform to the FDI Policy of the Government of India as announced from time to time and the Reserve Bank's Regulations/Directions issued from time to time.

End-use

DRs : While no end uses are specified, the existing bar on investments in stock markets and real estate would continue to be operative.

FCCBs : FCCB proceeds may be used for such purposes for which ECB proceeds are permitted to be utilised under the ECB schemes. However, FCCB proceeds cannot be used for investment in Stock Market.

Number of Issues

There is no restriction on the number of Euro Issues to be floated by a company or a group of companies in a financial year.

Warrants

Companies are not permitted to issue warrants alongwith their Euro Issue.

Repatriation of Proceeds

Companies may retain the proceeds abroad or may remit funds into India in anticipation of the use of funds, as approved.

Issue related expenses

DRs : The issue related expenses (covering both fixed expenses like underwriting commissions, lead managers charges, legal expenses and other reimbursible expenses) are subject to a ceiling of 4% in the case of non-listed DRs and 7% in the case the DRs are listed on US Exchange.

FCCBs : The issue related expenses should not exceed 4% of issue size and in case of private placement, 2% of the issue size.

Issue expenses beyond the ceiling would require RBI approval.

Reporting

After completing the transactions, the companies would be required to furnish full particulars thereof including amount of DRs/FCCBs issued, number of underlying fresh equity shares issued, percentage of foreign equity level in the Indian company on account of issue of DRs (stating whether under automatic route or with FIPB approval), detailed issue parameters, names of the overseas investors and number of FCCBs issued to each of them etc. to the Ministry of Finance, Department of Economic Affairs and the Exchange Control Department of the Reserve Bank of India, Central Office, Mumbai within 30 days of completion of such transactions.

WORKING MECHANISM OF DRS

Parties & Documents Involved in an Euro Issue (DRs)

Parties Involved*	Documents Involved*
Issuer	Information Memorandum
Merchant Bankers/Lead Manager	Subscription Agreement
Underwriters	Deposit Agreement
Overseas Depository	SEC Registration/Exemption
Domestic Custodian	Listing Agreement
Bankers	
Solicitors	
Auditors	
Investors	
*Illustrative	

The working mechanism of DRs is broadly summarised as under –

- ADRs / GDRs are issued on the basis of the ratio worked out by the Indian company in consultation with the lead manager to the issue.
- Indian company will issue its rupee denominated shares in the name of overseas depositary and will keep the shares in the custody of the domestic custodian appointed by the depositary.
- On the basis of the ratio worked out and the shares kept with the domestic custodian, the depositary will issue ADRs / GDRs abroad.
- Transfer & Redemption of ADRs / GDRs involve the following :
  - A non-resident holder of DRs may transfer those receipts or may ask the depositary to redeem those receipts.
  - In the case of redemption, the depositary would request Custodian to get the corresponding underlying shares released in favour of the non-resident investor.
  - Shares so released may be sold directly on behalf of the non-resident or transferred in the books of account of the issuer company in the name of non-resident.

  Therefore, overseas investors can trade in such ADRs / GDRs and at the same time may surrender their ADRs / GDRs. On surrender of ADRs / GDRs, the underlying shares are released in favour of the overseas investors; such shares may be held by investors or sold in the Indian markets.
- Under two-way fungibility scheme, effective February 13, 2002, shares released consequent to surrender of ADRs / GDRs and disposed of, can be reconverted into ADRs / GDRs.

CONCLUDING REMARKS

Euro Issue has been one of the important sources of fund raising for India Inc. Importance of Euro Issues has increased in recent times as more and more companies are approaching overseas markets to tap the required funds. Realising its importance, the Indian Government has liberalised the regulatory framework and put Euro Issues under the automatic route. However, lot of activities and documentation are involved in the process. Listing of DRs / FCCBs further increases the magnitude of the task. Thus, it is essential, especially for professionals like company secretaries, to be very well-versed with the Euro-issue mechanism and perform a value-added role not only on operational front but also on the broader aspects like strategy formulation and planning. ❑