

Sharing of the information between Debenture Trustee and Credit Rating Agencies

Recently SEBI has come out with a new circular [**Circular no. MIRSD/3/2013, dated 15th March 2013**] called sharing of information regarding issuer companies between Debenture Trustee and Credit Rating Agencies.

What is Debenture Trustee?

A debenture trustee is a person or entity that serves as the holder of debenture stock for the benefit of another party. When a company is looking to raise capital, one method of accomplishing this is by issuing stock as a form of debt with the obligation to repay the debt at a specific interest rate. The debenture trustee serves as a liaison between the company that issued the debentures and the debenture holders that are collecting interest payments.

When lending money through a debenture offering, an investor will receive a debenture certificate entitling him or her to a particular sum of money and a specified interest rate. As investors do not receive an individual bond for their investments, their loans are really a small portion of one large loan. This can be extremely risky in the event of a default as the smaller debenture investors may lose their entire investment. As a result of this, a debenture trustee is appointed when debenture stock is issued to a large number of investors.

When a large amount of debenture stock is issued, the company issuing the stock may be required to use its property as collateral. In this scenario, the property is mortgaged to the purchasers of the debentures and the deed is placed in a trust. The debenture trustee serves as the official representative for the debenture investors and is responsible for liquidating the collateral of the trust in the event that the company defaults on its debentures.

What is Credit Rating Agency?

A credit rating agency is a company that assigns credit ratings for issuers of certain types of debt obligations as well as the debt instruments themselves. A credit rating for an issuer takes into consideration the issuer's credit worthiness (i.e., its ability to pay back a loan), and affects the interest rate applied to the particular security being issued.

Credit ratings are used by investors, issuers, investment banks, broker-dealers, and governments. For investors, credit rating agencies increase the range of investment alternatives and provide independent, easy-to-use measurements of relative credit risk; this generally increases the efficiency of the market, lowering costs for both borrowers and lenders. This in turn increases the total supply of risk capital in the economy, leading to stronger growth. It also opens the capital markets to categories of borrower who might otherwise be shut out altogether: small governments, startup companies, hospitals, and universities.

What kind of Information can be share?

The above circular enables now, to share the information between Debenture Trustee's and Credit Rating Agencies regarding their client i.e., issuer company of debentures. The information normally contains two sides i.e., from credit rating agencies to debenture trustee's and from debenture Trustee's to Credit Rating Agencies.

1. Information from Credit Rating Agencies to Debenture Trustee's
 - a. Rating assigned/revised for debt securities along with the rationale for the same.
 - b. Press release, outstanding ratings etc. in respect of debt securities.
 - c. Non-cooperation by the issuers with respect to sharing necessary information for monitoring the credit quality of the rated instrument with CRAs.
 - d. Press release and separate communication to DT on withdrawal of rating post redemption of entire amount due towards debenture-holders.
 - e. Default of any type committed by the issuer.
2. Information from Debenture Trustee's to Credit Rating Agencies
 - a. Whether the asset in respect of which security has been created is free from any encumbrance and adequate to ensure asset cover for the debentures or if there is any breach of the terms of creation of the security. This information shall be shared on half yearly basis.
 - b. Funds transferred to Debenture Redemption Reserve (DRR), depletion of the DRR/invocation of guarantee which could affect the payment of debenture obligations. This information shall be shared annually.
 - c. Details of redemption of the issue.
 - d. Any default committed including the default in payment of interest or redemption of debentures or delay in creation of security.
 - e. Any change or restructuring of the terms of the issue.
 - f. Periodic reports from lead banks about the progress of the project for which funds have been raised through debentures and certificate from issuer's auditors in respect of utilization of funds.
 - g. Details of grievances filed by debenture-holders and action taken to resolve them.
 - h. Non-cooperation by the issuer with respect to furnishing required reports/certificates /information.

How to share the information?

The Debenture Trustee's and Credit Rating Agencies shall assign a separate e-mail ID for sending and receiving such information and ensure appropriate action, if any, based on such information received.

What is the effect of sharing the information?

Debenture Trustee's duty is protect the investor's fund. In case, Issuer Company tries to issue debentures by providing wrong information, it can be easily identified now. Debenture trustee can be cross check the Credit Rating Certificate with rating agency and obtain the rating information with any negative aspects, directly from credit rating agencies only.

The Credit Rating Agency can obtain the details in respect of any default in payment of interest on debentures or repayment of principle amount or breach of terms and conditions in related with issue, etc., directly from the Debenture Trustee. Therefore, now credit rating agencies can provide more accurate rating to the issuing companies.

Conclusion

By issuing this circular, SEBI has cross the another step to protect the investor's fund. Now, Issue Company should take more care about repayment of principles, payment of interest on debenture; comply with terms and condition of the issue, Credit Rating, etc.