# Companies may have to disclose source of funds coming via preferential allotment of shares

The securities market regulator plans to seek details of the source of funds flowing through preferential allotment of shares, a move aimed at deterring promoters from pumping money indirectly through front entities.

Two persons familiar with the matter told ET that the Securities and Exchange Board of India or Sebi's, move comes in the wake of increasing concerns over promoters or other investors channelising money into companies through complex structures involving interconnected entities.

"Sebi wants to know who is investing through certain front entities," said one of the persons quoted earlier.

The proposal was discussed by the 17-member Sebi Committee on Disclosures and Accounting Standards ( SCODA) on Friday. The committee, headed by Ishaat Hussain, director-finance of Tata Sons, has representatives from government bodies, corporates and investment banks.

Preferential allotment is a fundraising tool whereby companies issue equity shares, warrants or convertible instruments to promoters or any other investor. Such investors get preference over others, but such allotment entails a three-year lock-in period for promoters and a one-year lock-in period for other investors.

Financial sector regulators have been grappling with the issue of identifying the final beneficiaries or investors of transactions that involve multiple layers of bank accounts and investment vehicles. Legal experts, however, say Sebi may find it difficult to achieve its objective with this move.

"A requirement of disclosure of source of funds by a preferential allottee need not necessarily amount to disclosure of benami holdings or concerted action. If funds are routed through convoluted transactions or multiple layers, the disclosure of merely the last leg may not provide the true picture," said Akila Agrawal, partner at Amarchand Mangaldas, a leading law firm.

Existing norms require companies to disclose the name of the preferential subscribers, their permanent account numbers, number of shares proposed to be allotted and the price at which the shares would be issued.

"For most investors, subscribing to preferential issues through the normal banking channels (where banks require KYC details) and receiving shares in custody accounts, the source of funds rules will be a non-issue," said PR Srinivasan, managing partner, Exponentia Capital, a private equity firm.

Mehul Savla, director at Ripple-Wave Equity Advisors said the prevailing framework for preferential allotment has evolved over a period of time and adequate safeguards have been incorporated at each stage to deter misuse of this method of raising equity.

Investment bankers point out that preferential allotment is an effective and essential tool for the company to be able to raise funds, especially in challenging market conditions when the general sentiment is weak and there is limited appet ite from public investors.

Godrej Consumer Products had announced on Saturday a preferential issue worth $136 million to Singapore-based private equity firm Temasek Holdings.

(The Economic Times)