SEBI’s New Rule on Default

Why in news?

SEBI (Securities and Exchange Board of India) had asked listed companies to publicly disclose any default beyond 30 days.

What is the new rule?

- Default in repayment of principal or interest on loans from banks and financial institutions are to be disclosed.
- Such disclosure shall be made promptly, but not later than 24 hours from the 30th day of such default.
- In August, 2017, SEBI had issued a similar circular.
- It asked all listed entities to make such “disclosures within one working day from the date of default at the first instance of default.”
- However, SEBI had deferred the implementation of that rule hours before it was to come into effect on October 1 2017.
- The new default rule made now will come into force on January 1, 2020.

What is SEBI’s rationale?

- There is a gap in the availability of information, to different classes of investors, on defaults on loans by listed companies.
- Investors come to know of such defaults much later.
- Unlike this, a default on repayment of a bond or a similar instrument issued by a company has to be disclosed immediately.
- SEBI thus says the change was necessary to address this information asymmetry.
- An early disclosure can act as an early warning system.
- This can help investors make considered decisions on whether to stay on or sell the stock and exit, reducing their losses.
- In the current scenario, a meltdown such as those at IL&FS, DHFL, or PMC Bank, can leave many investors wary.
- It is thus expected that SEBI’s move will lead to greater credit discipline in the banking industry.
- **RBI’s move** - The RBI’s February 12, 2018 circular directed banks to start the process of resolution or restructuring of a loan even if the default was for only a day.

- The April 2, 2019 ruling of the Supreme Court striked down the circular.
- Following this, the RBI revised its rule in June 2019 offering a 30-day window to classify an account as a Non Performing Account.
- SEBI's circular now could be seen as a sign of regulatory synergy with the RBI.
- **Investments** - In 2017, SEBI restrained at the last minute on implementing the disclosure norms on default.
- But, 2018 and 2019 have seen the collapse of several corporates.
- Little was known about the true state of such companies before they went into bankruptcy.
- That too was based on anecdotal evidence with credit rating agencies way behind the curve.
- Resultantly, the erosion of faith could be detrimental to boosting fresh investment.
- It is now essential for both SEBI and the government to hold firm on the decision taken to instill confidence in investors and other stakeholders.

Source: Indian Express

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