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CROSS-LISTING OF SHARES: IMPLICATIONS AND THE ROAD AHEAD FOR INDIA

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ABSTRACT

Companies around the world keep treading innovative paths to increase investments and market value. Over the years, cross-listing has emerged as a viable mechanism for companies to improve market presence and gain global attention. Cross-listing of shares refers to the listing of shares on a different stock exchange other than the primary and original stock exchange. India followed a restrictive policy, wherein though Indian companies can list their debt securities on international exchanges (masala bonds), they can list their equity shares only through American Depository Receipt or Global Depository. In a similar manner, companies incorporated outside India could only access the Indian market through the depository route. With the accelerating pace of internationalization of capital markets and the rising need to attain global significance, India has deliberated some key changes to enable direct listing of equity shares of Indian companies in foreign exchanges. In 2018, the Securities and Exchange Board of India (SEBI) constituted a high-level committee to prepare a report and suggest plausible changes in the regulatory framework to realize this objective. The expert committee which submitted its report in 2018 has strongly advocated measures to implement direct cross- listing of shares of companies in India. In line with the report, several key amendments have been introduced in the regulatory framework. The move is predicted to be a game-changer in the Indian capital market scenario.

In this background, the research paper is an attempt to provide an overview of the regulatory changes initiated in India, and analyse its major impacts. The paper seeks to present a solution as to how the scheme can be implemented in the most feasible manner for the advancement of

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foreign investment in India and improving access to global markets for Indian companies.

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INTRODUCTION

In a world where corporate entities are vying for investments and improved visibility, cross-listing has emerged as a favourable investment mode for companies across the globe. Most importantly, it extends the crucial benefit of wider market access and recognition for corporate entities.[3] Additionally, companies incorporated in a jurisdiction with poor investor protection and enforcement mechanisms may also choose to commit themselves to greater corporate governance standards by cross-listing in other countries. While most countries have displayed an increasing alacrity to open up their stock exchanges, countries like China still continue to follow a restrictive policy in allowing access of their stock exchanges to foreign shares.[4] India, for a long time has been following a conservative approach to the practice, by allowing access to Indian stock exchanges only through depositories and conversely, permitting direct listing of equity shares in foreign stock exchanges only through American Depository Receipts (ADRs) or Global Depository Receipts (GDRs). In the recent past, India has realized the drawbacks inherent in its conservative practice of cross-listing that could significantly impede the globalisation of Indian capital markets. Consequently, significant amendments have been introduced in the Indian regulatory framework to adopt a liberalized practice of cross-listing. Though significant legislative changes have taken place, clarity on the scope of implementation has not yet emerged. The Government is still deliberating the rules for implementation of the legislative change in India. In this context, it is pertinent to analyse the implications of the proposed changes and study its important repercussions. The research paper is an attempt to comprehend the global practice in cross-listing, and correlate the same with the changes in the Indian regulatory framework to understand how the Indian practice can be best crafted to suit India's global ambitions.

[3] H K Baker, John R et.al., International Cross-Listing and Visibility, JOURNAL OF FINANCIAL & QUANTITATIVE ANALYSIS 495
(2002).
[4] Kamilla Sabitova, Impact of Cross-Listing on Companies Valuations: Evidence from Emerging Markets Impact of Cross-Listing on Companies Valuations: Evidence from emerging markets (2018).

UNDERSTANDING CROSS LISTING

One of the principal methods available for a company to raise money from the public is through listing of shares in stock exchanges. Every nation has a domestic stock exchange, where the shares of the companies incorporated in that country are listed and traded for money among the public. Cross-listing allows companies to simultaneously list their shares in multiple stock exchanges. Investors can buy shares of a company from a stock exchange and later trade them in another. Effectively, it obliterates the national boundaries in listing of shares and facilitates the internationalisation of domestic shares across boundaries.

Cross-listing has gained wide traction over the past few decades. Prompted by the increasing popularity of cross-listing among companies, scholars have tried to put out varying hypotheses to deduce the reasons motivating companies to cross-list their shares. Some of the prominent ones among these include the investor recognition hypothesis, market segmentation hypothesis, liquidity hypothesis etc. Investor recognition hypothesis is based on a deduction about investor sentiments. The supporters of the theory expound that increase in market value of a company is correlational with the awareness of investors about the securities.[5] Cross-listing which improves the visibility of a company at the global level, boosts investor awareness which in turn, results in an increased market value of the entity.

The market segmentation hypothesis is based on an analysis of market conditions. The increasing constrictiveness of markets, due to regulatory barriers can make investment tougher in the domestic market.[6] To overcome this, companies tend to cross-list to scatter the risk and compensate for the loss that may arise in the domestic market.

The liquidity hypothesis is based on the notion that improved liquidity of stock is one of the major reasons inducing companies to cross-list.[7] Cross-listing facilitates increased trading hours, thereby increasing the demand for the stock. The resultant competition among traders reduces bid-ask spreads and causes improved trading in the domestic markets.

Thus, it can be seen that the hypotheses present varying dimensions of the probable reasons that can prompt companies to cross-list. The hypotheses also give a glimpse into the purported

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[5] Olga Dodd, Why do Firms Cross-list their shares on Foreign Exchanges? A Review of Cross-Listing Theories and Empirical Evidence REVIEW OF BEHAVIORAL FINANCE p. 10-12 (2013).
[6] Id p. 4-8.
[7] Amir N. Licht, Cross-Listing and Corporate Governance: Bonding or Avoiding? CHICAGO JOURNAL OF INTERNATIONAL LAW (2003).

benefits of cross-listing. These include increased liquidity in the market, capability to raise capital at cheaper prices in a more efficient market, widening of shareholder base to expand financial risk and improved visibility and recognition in the investor market.[8] Nuanced approaches to the study of factors motivating companies to cross-list has also shown that familiarity with a neighbouring market also plays a dominant role in a company's choice of a market for cross-listing.[9] Geographic, cultural, and economic similarities and alikeness in stock exchange features with the home country can boost investor confidence to cross-list their shares in a given capital market.[10] While the factors that may influence a company to cross-list is largely subjective, the level of protection afforded within a particular corporate governance regime is found to be only a matter of secondar significance in most cases.[11]

The evolving ability of a market to attract foreign shares for cross-listing is usually considered as an indicator of a country's overall financial market activity.[12] From a development perspective, cross-listing can be a key catalyst for progress of nations, as its implementation may necessitate changes in both the home and target jurisdictions, along with transnational coordination, which in turn can promote comity among nations.[13]

However, in recent times, the notion that cross-listing leads to significant appreciation in the value of companies has been disputed through some empirical studies. The studies point out that in developed economies, where the domestic market itself has attained higher liquidity and integration, there is little incentive for companies to resort to cross-listing.[14] Statistics over the past few years indicate a decelerating trend among companies to cross-list shares.

Improvement in standards of corporate governance in home countries has also been pointed out as one of the major reasons behind this trend. [15] However, the study also reveals that cross-listing is still a lucrative option for companies in developing countries to access capital and

[8] G A Ndubizu, Do cross-border listing firms manage earnings or seize a window of opportunity? ,THE ACCOUNTING REV. (2007).
[9] Sergei Sarkissan, Michael J Schill, The Overseas Listing decision: new evidence of proximity preference, REVIEW OF FINANCIAL STUDIES (2004).
[10] Id.
[11] Supra note 5.
[12] Sarkissian, Schill, Cross-Listing Waves, THE JOURNAL OF FINANCIAL AND QUANTITATIVE ANALYSIS (2016).
[13] Larry E. Ribstein, Cross-Listing and Regulatory Competition, REVIEW OF LAW & ECONOMICS 97 (2005).
[14] Joanathan De Landsheere, Cross-listing in the 21st Century-Benefits of ADR-listings: an ending story?, TILBURG UNIVERSITY (2011-2012).
[15] Richard Dobbes, Marc H Goedhart, Why cross-listing shares doesn't create value, MCKINSEY & COMPANY (Nov.1, 2008), https://www.mckinsey.com/business-functions/strategy-and-corporate-finance/our-insights/why- cross-listing-shares-doesnt-create-value.

gain visibility at the international level. Despite the initial impact caused by the pandemic, capital markets in developed nations have managed to rebound to their initial levels and register spurts in domestic investment activities.[1644] Thus, the findings of these studies still remain relevant for the present analysis.

Cross-border listing can be executed primarily through two means. These include direct listing and indirect listing. In direct listing, companies directly offer their shares to the public without going through an IPO or with the aid of a facilitator such as banks. From an issuer's perspective, direct listing extends the benefit of limited expenses as compared to listing through an intermediary, which entails commission costs.[17] Indirect listing involves issuing of shares through depository receipts such as American Depository Receipts or Global Depository Receipts, evidencing the ownership of shares in companies of other countries. Indian companies may also list their debt securities on international exchanges in the form of masala bonds. As it exists, foreign companies seeking to cross-list in India can do so only through Indian Depository Receipts.[18] IDRs were introduced in India in the post-liberalisation era with the promulgation of the Companies (Issue of Indian Depository Receipts) Rules, 2004. The rules however prescribe higher standards for availing the facility that has made access to IDRs, largely an unviable option for potential investors.[19]

INTRODUCTION OF CROSS-LISTING IN INDIA

In 2013, the cancellation of the Bharati-MTN Merger, a $23-billion mega deal between Bharati Airtel and South Africa's MTN, which could have been India's biggest ever M & A transaction made headlines.[2048] When the South-African based MTN was not ready to forego its identity by totally merging with the Indian company, the Indian-based Bharti Airtel could not offer a solution to save the deal as the Indian regulatory framework lacked provisions which could have made the deal possible.

[16] Chris Bradley, Peter Stumpner, The impact of COVID-19 on capital markets, one year in, MCKINSEY & COMPANY (March 10, 2021), https://www.mckinsey.com/business-functions/strategy-and-corporate-finance/our-insights/the-impact-of-covid-19-on-capital-markets-one-year-in.

[17] Varma, Shelke, Direct Listing: The Beginning of Demise of GDR and IDR Routes, THE SCC ONLINE BLOG (Aug. 12, 2019), https://www.scconline.com/blog/post/2019/08/12/direct-listing-the-beginning-of-demise-of- gdr-and-idr-routes/.

[18] Nicholas, Vikaramaditya, Reverse Cross-Listings- The Coming Race to List in Emerging Markets and an Enhanced Understanding of Classical Bonding, CORNELL INT. L. J. (2014).

[19] Bhumesh Verma, Direct Listing: The Beginning of Demise of GDR and IDR Routes, SCC ONLINE (Aug. 12, 2019), https://www.scconline.com/blog/post/2019/08/12/direct-listing-the-beginning-of-demise-of-gdr-and-idr-routes/.

[20] Bharti-MTN deal may be biggest M & A in India's History, BUSINESS STANDARD (Jan. 19, 2013), https://www.business-standard.com/article/companies/bharti-mtn-deal-may-be-biggest-m-a-in-india-s-history-109052500173_1.html.

The merger could have led to the creation of the third largest telecom company in the world and also the single largest outbound FDIs from India.[21] The situation exposed a critical void in the Indian regulatory system that made the consummation of such a deal impractical. Numerous discussions arose in this context on the impending need to modernize the Indian approach to listing of shares and foreign investments.

It must be noted that the facility that could have come to the aid of the companies here is dual listing of shares as opposed to cross-listing. While cross-listing enables companies incorporated in India to directly list their shares oversees before or after listing in India, dual listing permits listing of shares overseas only after listing in the domestic capital market.

Merging through dual listing takes the form of a dual listed company (DLC). A dual listed company comprises two legal entities functioning as a single business.[22] By mutually listing their shares on the stock exchanges in the respective jurisdictions, the two companies synchronise their operations as a single entity, while maintaining their individual identities.

In cross listing, the cross-listing firm maintains a single identity.[23] For instance, consider that a firm has listed in stock exchanges A and B. Buying shares from A will be equalent to buying from B. Consequently, the share purchase process will be interconvertible, which means the shares bought in A can be sold in B.

Though cross-listing appears to present a more liberal approach, dual listing is often preferred over cross-listing due to various reasons. Dual listing comes with the benefit of eased tax burdens. In an ideal merger scenario, the acquirer company is put to bear a huge tax burden in proportion to its capital gains from the merger. As a merging of operations through cross-listing does not lead to accumulation of a vast proportion of capital assets in one company, the tax burden is equitably shared by the merging entities.[24] The prospect of not losing individual identities in the merging process also makes dual listing, an attractive option for

[21] Sandeep Joshi, Bharti Airtel calls off merger talks with MTN, THE HINDU (Sept. 30, 2009), https://www.thehindu.com/business/Industry/Bharti-Airtel-calls-off-merger-talks-with- MTN/article16884239.ece.
[22] Dual Listing-When a company's shares are listed on more than one stock exchange, CORPORATE FINANCE TRAINING, https://corporatefinanceinstitute.com/resources/knowledge/trading-investing/dual-listing/.
[23] David Kimberly, How do dual listings work? FREE TRADE (Oct. 25 2021), https://freetrade.io/learn/how-do- dual-listings-work.
[24] Anand Rawani, SundayET Guidebook: What is dual listing, THE ECONOMIC TIMES (Oct. 4, 2009), https://economictimes.indiatimes.com/money-you/sundayet-guidebook-what-is-dual-listing/articleshow/5085349.cms?from=mdr.

companies.[25]

The spike in discussions that followed the failure of the Bharti-MTN deal brought to the fore, the issue of internationalisation of Indian share markets. In 2014, the Government permitted unlisted Indian companies to raise capital in international capital markets without listing in India for a period of two years initially through an amendment to the Foreign Direct Investment (FDI) policy. After about four years, the Securities and Exchange Board of India constituted a 9-member expert committee to review the matter and suggest plausible methods for implementation of the scheme in India. The expert committee report was submitted in December,2018. It contained elaborate provisions for introducing cross listing in India. It suggests certain key amendments to legislations such as the Companies Act, 2013, Foreign Exchange Management Act, 1999 (FEMA), the Income Tax Act etc. to effectuate cross-listing in India.

For a country that has been practicing a restrictive approach to the listing of shares for a long time, despite the changing trend around the world, a decision to allow cross-listing of shares in a renewed regulatory atmosphere is a bold stance. It is notable that while recommending such a drastic change in the policy, the Expert Committee has also carefully considered incorporation of some safeguards to tackle any misapplications of the permissive provisions. Accordingly, it proposes that Indian companies can resort to direct listing of shares only in certain specified jurisdictions identified as "permissible jurisdictions."[26] A permissible jurisdiction is identified as a jurisdiction with which India has treaty obligations to share information and cooperate for investigations.[27] Complementing the status, the committee also recommends that the country must be a member of the Board of International Organization of Securities (IOSCO), and Financial Action Task Force (FATF) or any other jurisdiction notified by the Central Government following consultations with the Securities and Exchange Board of India (SEBI) upon an appraisal of the jurisdictions' capital market regulations. Special emphasis has been given to exclude jurisdictions having inadequate regulatory frameworks to counter money-laundering or terrorism. The qualifications primarily lay down tougher standards, which are difficult to satisfy. Scholarly studies estimate that the tougher

[25] *Id.*
[26] SECURITIES AND EXCHANGE BOARD OF INDIA, REPORT OF THE EXPERT COMMITTEE FOR LISTING OF EQUITY SHARES OF COMPANIES INCORPORATED IN INDIA ON FOREIGN STOCK EXCHANGES AND OF COMPANIES INCORPORATED OUTSIDE INDIA ON INDIAN STOCK EXCHANGE (December 4, 2018).
[27] *Id.*

standards can lead to exclusion of many major jurisdictions as opposed to inclusion.[28]

In September 2020, the Government notified the Companies (Amendment) Act, 2020, which has introduced provisions permitting direct listing of shares out of India. Section 23 of the Companies Act has been amended to provide for issuing of shares in international markets. As recommended by the Expert Committee, such listing of securities is allowed only in capital markets of "*permissible foreign jurisdictions or such jurisdictions as may be prescribed*" in that regard. Thus, the legislature has taken care to ensure that safeguarding provisions are put in place to curtail misuse of the permissive provisions. Perhaps, the initial restrictive approach to cross-listing might serve as a prelude to the introduction of a liberal cross-listing regime in India in future. While the parent legislative changes have been introduced, ancillary rules laying down the implementation mechanism of cross-listing are still awaited.

Recently, there have been speculations that the government is deliberating legalisation of only dual listing of shares in India. While concerns abound about the possible division in liquidity between countries that dual listing can cause, some also identify it as a more prudent measure for India's business atmosphere. The most common concern raised against cross-listing is that it can lead to export of capital from India as Indian companies seeking overseas operations can directly list shares abroad without primary listing in India.[29] Due to the reciprocal benefits that cross-listing entails, experts fear that it can only benefit overseas companies in the long run.[30] Clarity on the scope of implementation of these changes cannot emerge until the relevant regulations are promulgated. Given the fact that India is still at a nascent stage with respect to these changes, dual listing may be a more practical option for India to gain a foothold in this sphere.

Along with the major policy change, India must also equip itself with sturdy mechanisms to balance the multifaceted reforms with the challenges which could arise in the background of the adoption of a liberal investment policy. This requires increased coordination with the foreign jurisdictions[31] and extension of reciprocal benefits to stimulate good foreign relations.

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[28] Padma Singh, Cross Listing: Benefits Beyond Borders, JOURNAL OF ADVANCED & SCHOLARLY RESEARCHES IN ALLIED EDUCATION (2019).
[29] Tarush Bhalla, Jayashree P Upadhyay, Overseas listing draft norms may have an option of 'dual listing, MINT (Sept. 11, 2020), https://www.livemint.com/market/stock-market-news/overseas-listing-draft-norms-may-have-an-option-of-dual-listing-11599837365171.html.
[30] *Id.*
[31] Gautham Srinivas et.al. India: Overseas listing of Indian Companies, MONDAQ (May 13, 2020), https://www.mondaq.com/india/shareholders/932794/overseas-listing-of-indian-companies.

Further, there must be a co-extensive extension of the extra-territorial jurisdiction of the SEBI to empower the regulator to effectively pre-empt or control manipulative acts, which could cause a misuse of the enabling provisions.[32] In this regard, the Supreme Court's ruling in *Securities and Exchange Board of India v. Pan Asia Advisors Ltd. & Anr.*[33] is instructive. In this case, the Apex court held that the Indian capital market regulator has jurisdiction to investigate into the matter of GDRs sold by Indian companies over foreign exchanges. The case related to a finding of the SEBI against a merchant financing firm, Pan Asia Advisors Ltd. that it had committed fraud on the Indian investors and drew undue benefits by manipulating the Indian shares. The regulator proceeded to debar the firm from accessing the capital market in India directly or indirectly for a period of 10 years. The relevant order was challenged. In a landmark decision, the Apex Court ruled in favour of extending SEBI's jurisdiction based on internationally recognized principles such as the "effects doctrine" and appreciation of the legislative wisdom behind the enactment of the SEBI Act, 1992, which establishes the regulator. The court observed that in its role as a sectoral regulator tasked with the function of protecting investors and stock markets in India, the SEBI has the necessary jurisdiction to adopt measures for curtailing such practices which it deems contrary to the interests of Indian investors and security market. While observing so, the court also placed reliance on the definition of fraud within the provisions of the relevant regulations pertaining to GDRs. Thus, it is important to realize that statutory backing is essential to give teeth to the regulatory provisions. Therefore, while cross-listing is introduced in India, necessary changes must also concurrently take place in the relevant governing regulations, especially regarding the functions of SEBI to make the system fool proof.

India must be also vigilant to ensure that the situation that ensued after the promulgation of the IDR Rules in 2004 does not reoccur after the introduction of cross-listing. The IDR rules laid down that the companies seeking to issue IDRs in India must have a pre-issue paid up capital and free reserve of at least USD 50 million and a minimum average market capitalization of USD 100 million in the parent company during the past three years. The stricter qualification criteria prescribed under the rules effectively deterred potential foreign companies from issuing IDRs in Indian stock markets. Consequently, it was only after five years from the promulgation of the rules that India received its first ever IDR issue from Standard Chartered Bank.[34] Such a condition can render the reforms meaningless and

[32] *Id.*
[33] Securities and Exchange Board of India v. Pan Asia Advisors Ltd. & Anr, [2015] SCC OnLine SC 626.
[34] Supra note 9.

immature. The immediate focus should be also on ensuring that the intended beneficiaries derive adequate benefits from the major policy changes.

BENEFITS FROM CROSS LISTING

The rationale for utilizing "liquidity pools" is weak as any institutional investor interested in investing in Indian stocks must register as a foreign institutional investor (FII) in order to purchase their shares.[3563] Moreover the major international brokerage firms having presence in India provide coverage of the companies of interest to investors. It is therefore wrong for these organizations to carry out further evaluations as they have stronger governing standards. Also, nowadays, corporate practices are becoming more and more integrated in terms of disclosuresand increasing partnerships with investors. Thus, Companies need to determine whether the nominal benefit they expect from the cross-listing of their securities is worth the compliance costs associated with cross-listing. Another benefit for companies occurs in the form of higher visibility and global presence, which can be beneficial for extending brands or activities into new areas more efficiently. A secondary listing may provide owners with greater investment diversification, increased liquidity, and perhaps lower investment risk because the shares are exposed to two or more markets rather than just one.

The benefits of cross listing can be analysed on the basis of benefits to the Indian economy and benefits to companies incorporated in India. To date, foreign investors have always benefited from the surge in Indian stocks. While it is true that Indian investors have also experienced the same, they still need to diversify their investments. Such entries help in the globalization of our currency, strengthen our financial position, create better laws, and nurture a professional service environment. This helps the local market, because in such cases it is worthwhile to include more emerging markets in the list. The companies incorporated outside India in partnership with the brand "India" have been fruitful as the Indian market is full of potential that the outside companies can reap. Further by gaining access to the Indian market, outside companies can derive benefits from a wider base of consumers and market participants. As far as Indian investors are concerned, portfolio diversity has increased where eligible investors of India may like to invest in the stock of global blue-chip businesses, and the planned liberalisation of the Indian regulation is an operative means of granting their wishes. Participation in the wealth generated by multinational corporations would also allow Indian investors to participate in the wealth generated by multinational enterprises that have

[35] Supra note 28.

a substantial impact on Indian lives if they were to invest in the equity share capital of companies incorporated outside India. Hence, its high time for multinational companies reaping benefits to share the gains by issuing shares.

CONCLUSION

Though the global trend in cross-listing of shares is receding, for a developing nation like India, enabling cross-listing of shares is a positive move. During the financial year 2015-2016, Indian companies for the first time in 25 years recorded zero raising of funds through overseas equity offerings, which heralded a decreasing popularity of ADRs/GDRs among Indian firms as viable investment routes.[36] The introduction of direct cross-listing of shares coupled with the pressing need for internationalization in the modern days, could possibly revive the enthusiasm of Indian firms to globalize their activities. Legalisation of cross-listing could be a boon to start-ups in India as it comes with the benefit of a diverse listing option and safer investment options.

As it is evident, introduction of cross listing has the potential to propel the Indian economy to new heights, while also ensuring that the brand "India" gets an adequate share of the financial market. It also enhances the credibility and popularity of Indian companies at the global level. However, it also comes with an overarching need to revisit almost all laws containing implicit or explicit provisions dealing with foreign investments or trade. Given the current crisis, which has made a relook into legislative provisions in almost all domains of law practically inevitable, these changes are not easy to come by. Though the Expert Committee constituted by the SEBI has laid the foundation for the law, laying down the law in letter and spirit may require more comprehensive consultations and review at multiple levels. In this context, the moderate and slow approach adopted by the government to implement the changes reflects prudence and appreciation of the complexity of the issue on part of the executive. While a gradual change is preferred, care must also be taken to put in place robust mechanisms and complementary policy changes, which will make the reform more meaningful and conducive for India's business atmosphere.

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[36] 64 Rajesh Mascarenhas, Indian companies didn't raise funds through overseas equity offerings during FY15, THE ECONOMIC TIMES (March 28, 2016), https://economictimes.indiatimes.com/indian-companies-didnt-raise-funds- through-overseas-equity-offerings-during-fy15/articleshow/51577096.cms.