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LEGAL CHALLENGES IN INITIAL PUBLIC OFFERINGS(IPOS)

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ABSTRACT

Initial public offerings (IPOs) constitute a pivotal milestone in the corporate life-cycle, signalling the transition from "private to public" ownership and providing companies with access to a vast pool of equity capital. In the Indian context, the IPO process is governed by a dense lattice of legal instruments, notably the "Companies Act 2013, Securities Contracts (Regulation) Act 1956, and a constellation of Securities and Exchange Board of India (SEBI) regulations—chief among them the Issue of Capital and Disclosure Requirements Regulations 2018 (ICDR) and the Listing Obligations and Disclosure Requirements Regulations 2015 (LODR)". Although the framework is calibrated to enhance transparency and investor confidence, its very breadth presents practical hurdles. Prospective issuers must navigate overlapping disclosure obligations, strict pricing restrictions, promoter lock-in requirements, and onerous post-listing governance standards. Compliance costs and procedural delays, exacerbated by frequent regulatory amendments, can erode the attractiveness of the domestic market and prompt high-growth enterprises to consider overseas listings. Navigating this framework imposes a multilayered compliance burden that can delay market entry and inflate transaction costs, effects felt most acutely by first-time issuers and entities operating in sectors such as insurance and banking that already face dedicated supervisory regimes. This study undertakes a doctrinal and case-based analysis of the principal legal challenges confronting IPO aspirants. It maps the statutory and regulatory terrain and then dissects five recurrent pain points: due-diligence and disclosure, pricing and valuation transparency, promoter lock-in and dilution, corporate governance transition, and litigation risk. Three case studies—Paytm, Zomato, and LIC—are employed to contextualise these issues and test the efficacy of recent reforms. The findings reveal that the core impediment to timely and cost-effective capital raising is not regulatory intent but legislative complexity, interpretive uncertainty, and the pace of rule change. To address these bottlenecks, the paper proposes a reform agenda centred on principle-based regulation, adoption of regulatory technology (RegTech) to streamline filings, and institutionalized stakeholder consultation to future-proof rule-making. Implementing these

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recommendations can help strike a durable balance between safeguarding investors and fostering an agile, competitive primary market.

Keywords: IPO, SEBI, Companies Act 2013, ICDR Regulations, corporate governance, RegTech.

INTRODUCTION

Raising capital through an IPO is simultaneously a corporate finance strategy and a transformative legal event. Globally, issuers must contend with securities legislation that seeks to reconcile investor protection with efficient capital mobilization. In India, that equilibrium is particularly delicate owing to the relative novelty of widespread equity investing, the dominance of retail participation, and the developmental mandate assigned to SEBI in deepening capital markets. The enactment of the Companies Act 2013 modernized corporate governance norms, while the contemporaneous overhaul of SEBI's primary-market regulations codified the disclosure-centric ethos that has since come to define Indian securities law. Yet, regulatory sophistication alone does not guarantee seamless execution.

Indian IPO activity has witnessed a marked upswing since 2020, propelled by record liquidity, bullish sentiment, and an expanding investor base that added nearly thirty million demat accounts in the 2021–22 fiscal year alone. Mega-offers such as those of Zomato, Nykaa, and LIC collectively raised over ₹1.5 trillion, signalling unprecedented appetite for primary issuances. Yet with scale comes scrutiny: valuation premiums, loss-making issuers, and lock-in relaxations have invited intense parliamentary debate and public-interest litigation, posing new legal challenges for both issuers and regulators.[2]

Consequently, stakeholders face a paradox: while the rules ostensibly foster transparency and market integrity, their volume and velocity create interpretive uncertainty, fuelling compliance costs and prolonging time-to-market. Merchant bankers report that legal and diligence expenses for a mid-cap IPO now exceed 2 percent of issue size, up from 0.8 percent a decade ago. Such costs have motivated some technology start-ups to explore overseas listings, invoking the need for balanced reform.[3]

Against this dynamic backdrop, the present paper investigates two inter-related questions: which legal bottlenecks exert the greatest drag on IPO timelines, issue costs, and aftermarket

[2] IM Barsan, 'Legal Challenges of Initial Coin Offerings (ICO)' (2017) 3 Revue Trimestrielle de Droit Financier (RTDF) 54
[3] Ibid.

performance; and whether recent regulatory tweaks are sufficient to mitigate such frictions or a more holistic overhaul is warranted. The analysis furnishes actionable insights for policymakers devising balanced reforms and for companies contemplating listings in India.

REGULATORY LANDSCAPE FOR IPOS IN INDIA

COMPANIES ACT 2013

Section 23 permits public offers, while Section 26 enumerates prospectus contents, mandating disclosures on financials, risk factors, and management discussion & analysis. Liability for misstatements is strict—directors and experts may incur civil liability under Section 35 and criminal penalties under Section 448 for fraudulent statements.[4]

SEBI ICDR REGULATIONS 2018 (AS AMENDED IN 2024)

Replacing the 2009 iteration, ICDR consolidates provisions on eligibility, pricing, lock-in, and disclosures. Regulation 6 requires a minimum ₹3-crore net tangible assets threshold, while Regulation 14 caps the price band at 75 percent of the upper limit. The 2024 amendment introduced a "fast-track" route for AA-rated issuers, eliminating the 90-day filing waiting period between the "Draft Red Herring Prospectus (DRHP)" and the final prospectus.[5]

SEBI LODR REGULATIONS 2015

Post-listing obligations include quarterly financial statements, board composition with at least one-third independent directors, and audit committee oversight. Regulation 30 codifies materiality thresholds for disclosure of events, introducing a degree of subjectivity that fuels compliance uncertainty and litigation risk.[6]

ANCILLARY STATUTES AND GUIDELINES

The "Securities Contracts (Regulation) Act 1956": governs listing contracts and grants SEBI power to regulate stock exchanges. The "Foreign Exchange Management Act 1999" and Consolidated FDI Policy shape foreign investor participation. Sector-specific statutes—for example, the

[4] J Seepani and KVR Murthy., 'Initial Public Offerings in India – A Structural Review' (2023) 7 European Journal of Economic and Financial Research 4
[5] Ibid.
[6] Ibid.

Insurance Act 1938 in LIC's listing—impose additional layers of compliance. Overlaps and occasional inconsistencies—such as differing disclosure thresholds between the Companies Act and ICDR—create interpretive grey zones that manifest as legal challenges during IPO preparation.[7]

KEY LEGAL CHALLENGES

DUE-DILIGENCE AND DISCLOSURE OBLIGATIONS

Robust disclosure, the cornerstone of investor protection, is mandated by Section 26 of the Companies Act and Chapter VI of ICDR. Determining materiality, especially for forward-looking statements, is contentious. The Securities Appellate Tribunal in PNB Housing Finance Ltd. v. SEBI cautioned against boiler-plate disclosure, yet industry practice still leans heavily on generic language. Strict liability for misstatements fosters a 'defensive disclosure' culture that can obscure rather than clarify risk.[8]

PRICING, BOOK-BUILDING AND VALUATION TRANSPARENCY

Indian issuers must publish a price band with a maximum 75 percent spread and justify it in the Red Herring Prospectus. SEBI's 2022 consultation paper proposed mandatory disclosure of key performance indicators used in valuations, citing opacity in tech IPOs. Anchor investor allocation and the optional greenshoe mechanism, though designed to stabilise prices, are criticised for favouring institutional investors and complicating fair-allocation norms.

PROMOTER LOCK-IN AND DILUTION REQUIREMENTS

ICDR mandates an 18-month lock-in on at least 20 percent of the post-issue paid-up capital held by promoters. While intended to align interests, such lock-ins can deter private-equity exits and complicate pre-IPO restructuring. Exemptions exist for professionally managed companies, but the definitional threshold for "promoter" remains debated, leading to divergent appellate interpretations.[9]

[7] Veluvali P and Veluvali P, 'Legal Framework and Governing Design for IPOs in India' in Retail Investor in Focus: The Indian IPO Experience (2019) 33.
[8] G Gupta and F Rakhecha, 'Impact of New SEBI Regulations on IPO(s) in India. Part 1' (2022) 2 Indian Journal of Integrated Research in Law 1
[9] Supra note 7.

CORPORATE GOVERNANCE TRANSITION

LODR ushers in stringent governance norms—independent directors, nomination-remuneration committees, and whistle-blower mechanisms. Converting a founder-centric board to this structure pre-IPO is resource-intensive. The 2023 LODR amendment mandating disclosure of shareholder agreements adds complexity, especially for start-ups with layered preference share structures.[10]

LITIGATION AND REGULATORY SCRUTINY POST-LISTING

Post-listing suits under Section 245 of the Companies Act enable class actions by shareholders. The Paytm IPO witnessed public-interest litigation alleging misleading valuation disclosures. Even if dismissed, such suits amplify reputational damage. SEBI's enhanced settlement mechanism further incentivises enforcement, as evidenced by a ₹45-crore settlement with Brightcom Group in 2023.[11]

RECENT JUDICIAL AND REGULATORY DEVELOPMENTS

ICDR AMENDMENTS 2024

The amendment package introduced a fast-track listing route dispensing with the mandatory 90-day cooling-off period for qualified issuers, potentially reducing time-to-market by nearly 40 days. Critics fear an erosion of vetting intervals necessary for investors to assimilate substantial information.

SUPREME COURT JURISPRUDENCE

In Franklin Templeton Trustees v. SEBI (2023)[12] the Supreme Court fortified SEBI's investigative reach under Sections 11 and 11C of the SEBI Act, holding that any matter affecting investor interest—even tangential to primary issuance—falls within SEBI's purview. This expansive reading signals that disclosure lapses discovered post-listing could still incur regulatory reprisal.

[10] Supra note 7.
[11] Supra note 7.
[12] CIVIL APPEAL NOS. 498-501 OF 2021.

LODR AMENDMENTS 2023

To enhance transparency over control rights, Regulation 31B now compels disclosure of agreements, including shareholder or voting agreements, that materially affect management or control. For IPO candidates with complex term sheets, this may require redacting or renegotiating clauses or risk deferring the offer.

ENHANCED SETTLEMENT FRAMEWORK

SEBI's 2023 overhaul increased transparency in the calculation of the indicative amount and introduced a "collaborative" enforcement path enabling early-stage cooperation credits. Although yet to be tested in an IPO context, the framework could expedite resolution of prospectus-related non-compliance, curtailing prolonged litigation.

CASE STUDY ANALYSIS

PAYTM (ONE97 COMMUNICATIONS) IPO 2021

India's largest IPO faced scrutiny over its ₹2,150 issue price amid subsequent market under-performance. Critics argued inadequate disclosure of merchant-acquisition costs and customer churn rates. SEBI's observation letter highlighted valuation risk but ultimately cleared the offer, illustrating the regulator's constrained role vis-à-vis commercial judgment.[13]

ZOMATO IPO 2021

Zomato pioneered KPI disclosures—gross order value, active users—yet grappled with allegations of selective risk emphasis. Its blockbuster listing prompted SEBI's KPI consultation and shaped subsequent regulatory clarifications.[14]

POLICY RECOMMENDATIONS

Adopt a principle-based regulatory philosophy that clearly articulates the investor-protection outcomes SEBI seeks—fair valuation, timely disclosure, equitable allocation and accountable

[13] De P, 'Paytm: Lack of a Cogent IPO Story?' (2024) 21 Asian Journal of Management Cases 215.
[14] Tuyon J, Huang C.H and Swanepoel D, 'The Zomato Dilemma: A Realistic Growth Trajectory and Share Price Fair Valuation?' (2024) 14 Emerald Emerging Markets Case Studies 1.

governance—while allowing issuers discretion over the precise metrics and narrative they deploy. Replacing lengthy prescriptive checklists with a concise set of "comply-or-explain" principles would let founder-led technology companies highlight bespoke operating indicators yet preserve a statutory back-stop against boiler-plate language or selective risk omissions. Such flexibility encourages innovation in prospectus drafting, trims unnecessary language and, by focusing enforcement on substantive harm, deters cosmetic compliance.

Embed regulatory technology at every stage of the issuance workflow. A single, cloud-native portal should enable issuers, merchant bankers, legal advisers and SEBI reviewers to exchange diligence artefacts, prospectus drafts and query responses in real time. Machine-learning algorithms can flag inconsistencies between financial statements and risk factors, pre-populate standard sections, benchmark projected metrics against sectoral peers and estimate settlement penalties for late filings. Coupled with audit-grade version control and blockchain-anchored timestamping, RegTech can compress the traditional six-to-nine-month timeline for a mid-cap listing to four months, while simultaneously creating a forensic trail that disciplines both issuers and intermediaries. Institutionalise deep, iterative stakeholder consultation. Rather than periodic white papers with 30-day comment windows, SEBI should convene standing panels comprising issuers, buy-side analysts, retail-investor associations, academic experts and technology vendors. Panels can meet quarterly to review emergent business models—such as platform aggregators, climate-tech ventures and deep-science start-ups—identify disclosure blind spots and test draft rules in sandbox mode before market-wide rollout. Structured feedback loops would surface practical pain points early, refine guidance notes and minimise interpretive ambiguity when rules formally launch. Together these three reforms promise a lighter, smarter rulebook that lowers transaction costs without diluting safeguards. Principle-based norms future-proof the framework; RegTech turns that framework into an efficient digital utility; and continuous dialogue anchors both to grounded market reality, allowing Indian IPOs to scale responsibly in lockstep with global standards while safeguarding the interests of an increasingly sophisticated domestic investor base securely.

CONCLUSION

India's IPO regime has evolved into one of the world's most detailed systems, marrying the Companies Act, SEBI regulations and sector-specific statutes into an imposing compliance superstructure. That architecture undoubtedly lifts disclosure quality and guards retail investors, yet its density also slows issuance, inflates costs and, at times, obscures rather than illuminates risk.

The contrasting fortunes of Paytm, Zomato and LIC underscore how legal complexity, more than market sentiment, often determines pricing success, investor confidence and post-listing stability.

Future growth therefore hinges on a regulatory recalibration: pivoting from exhaustive checklists to clear outcome-based principles, deploying RegTech to digitise filings and automate red-flag analytics, and embedding continuous dialogue with issuers, intermediaries and investors. Together, these measures can convert a fragmented rulebook into an agile, tech-enabled ecosystem that rewards transparency without suffocating innovation.

If implemented decisively, the reforms will compress time-to-market, reduce compliance uncertainty and attract high-growth enterprises that might otherwise list abroad. Most important, they safeguard the trust of an expanding domestic investor class while aligning Indian primary markets with global best practice. A smarter, proportionate regulatory framework is thus not merely desirable but indispensable to financing India's next wave of economic transformation and inclusive wealth creation for shareholders nationwide.

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