

# DISCLOSURES OF KEY PERFORMANCE INDICATORS IN OFFER DOCUMENT

## Abstract

*The amendments made to the Securities Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018 [SEBI ICDR] dated 21st November, 2022 included certain provisions of great relevance to the profession of CMA mandating disclosure of Key Performance Indicators (KPI) in the offer document under the section dealing with “Basis for Issue Price” in addition to disclosures of financial indicators. This article after giving a brief introduction to the subject covers the amendments in the regulatory framework.*



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***“If you can’t measure it, you  
can’t improve it”***

**- Peter Drucker**

## INTRODUCTION

**S**EBI has taken various steps from time to time to strengthen the quality and standards of disclosures for the purpose of ensuring dissemination of information in a transparent manner to all the investors. The regulations relating to disclosures and reporting with respect to the issue of capital in the primary market are mainly contained in Schedule VI to the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018 (hereinafter referred to as SEBI

ICDR). Significant amendments which are of great interest and relevance to the CMA professionals were made to the SEBI ICDR vide the Fourth Amendment Regulations dated 21<sup>st</sup> November 2022 providing for the first-time detailed regulations with respect to disclosures relating to “Key Performance Indicators” (KPIs) in the offer document under Section K – Basis for Issue Price. In this article the concept of KPIs is briefly explained and an attempt is made to highlight the salient points of the new requirements arising out of the SEBI amendments concerning the KPIs.

## UNDERSTANDING KPIs

Peter Drucker, a renowned management expert, is known to have said “What is measured gets done”

thereby highlighting the importance of measurement of performance from a strategic perspective. Measurement of performance is of vital importance to ensure that the work and processes carried out are effective in creating the desired impact and in case of any lag it helps to focus on the measures required to be taken for improvement. These measures relating to performance may be with reference to inputs or resources utilised, processes, outputs, outcomes or even project milestones.

When drilled down and analysed, it is noticed that the term KPI has three powerful words namely “key”, “performance” and “indicators.”

An “indicator” refers to a measure used to quantify performance with reference to a particular parameter. For example, merely computing total

labour hours worked over a month in a manufacturing unit by itself does not convey any meaning. But when related to the total labour hours available in the month in the said unit, it helps the management to assess the idle time or the extent of capacity utilisation.

A “performance indicator” is a quantitative or qualitative measurement or other criterion against or by which performance or achievement of a person, department or company is assessed usually against a target, standard or a budget. Thus, in the cited example, if it is targeted to contain idle time to 10 per cent and the actual measurement in the given period is 15 per cent, this 15 per cent against 10 per cent is a performance indicator

Now all performance indicators are not “key performance indicators”. To qualify as a “key performance indicator”, the performance indicator should be among the most critical indicators for success at the highest level of strategic management. KPIs are those measures that are used to assess and evaluate the progress made towards achieving the strategic business goals. In the cited example, if the unit is operating at a high break-even point level, maximising capacity utilisation and minimising controllable idle time could be two of the KPIs.

Typically, most strategic teams track around 20 to 25 KPIs that span across four broad perspectives namely financial, customer, process and people.<sup>1</sup>

### Key steps in the KPI process



Source: <https://www.techtarget.com/searchbusinessanalytics/definition/key-performance-indicators-KPIs>

### QUALITIES OF GOOD AND EFFECTIVE KPIS

The process of setting KPIs requires a thorough understanding of the various business functions, activities and processes so as to be able to identify the key success variables that have a closely measurable correlation with the success and sustainability of the business of the company. Having said this, the qualities of good and effective KPIs can be aptly summarised by the acronym “RAMA”.

**Realistic:** It is obvious that KPIs should be realistically attainable; otherwise they may remain as pipe dreams contributing to internal bickering, one-upmanship and other negativity within the organisation thus doing more harm than

good. A proper balance should be established when setting ambitious and yet practically achievable KPI targets that motivate that extra effort in the organisation.

**Aligned to the Objective:** KPIs should be aligned to the overall business objective, goal, outcomes and strategies. Thus, for a sales and marketing team enquiry conversion or strike rate could be a KPI because higher strike rate would contribute to a higher revenue.

**Measurable:** KPIs are incomplete without they being capable being measured with reasonable accuracy. Now that there are various tools of data analytics to choose from, this should not be a constraint.

**Actionable:** The purpose of setting KPIs should be to seek continuous improvement and this calls for outlining the steps required to be taken to reach the targeted KPI levels. Thus, good and effective KPIs are those that inspire positive action.

### Common Mistakes in Choice of KPIs

Some of the common mistakes that are continued to be made in the choice of KPIs can be classified into two categories namely -

- ⊙ *Choosing KPIs that has been historically measured, so-called time tested and therefore should be continued as KPIs.* In a rapidly changing dynamics of the economics of business environment and with the availability of advanced data analytics and AI tools, relevant information is the key to success.

Given the availability of relevant information, the KPIs should be subject to review and should be modified to fit into new realities as a continuing exercise.

- ⊙ *Choosing KPIs that are simple, easy to understand and easy to measure.* Though being simple and easy to understand and / or measure with respect to a KPI is a great virtue, over emphasising on simplicity rather than on attention to being relevant to strategy can lead to meaningless results. This is particularly the most likely scenario when decision making is based on KPIs that are not in alignment with strategy.

### Making KPIs Work

Introducing KPIs at the workplace is not free from challenges. If KPIs are used as tools for enforcement of performance, any success achieved will be short-lived and not sustainable in the long run. KPI systems instead work better in organisation that places more emphasis on the right approach and processes rather than on achieving results with the latter being any way not guaranteed. The right approach would be to create a right MRI (monitoring, reporting and improvement) culture which motivates managers at all levels as well as the staff and workers to put in their best efforts. This is not difficult to achieve if the processes are backed by a strong performance management system that is consistent, simple and transparent. The performance management

<sup>1</sup> <https://www.clearpointstrategy.com/18-key-performance-indicators/>

system should provide for assigning responsibility for each KPI to specific department / managers to track and report the progress. Periodicity should be defined for reporting on the performance be it daily, fortnightly, monthly or quarterly. Regular monitoring and reporting is the key to make KPIs work with the focus being on improving performance rather than on enforcement of performance.

## OVERVIEW OF REGULATORY REQUIREMENTS

The SEBI ICDR was amended on 21<sup>st</sup> November, 2022 to provide for regulations with respect to KPIs vide the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) (Fourth Amendment) Regulations, 2022. The salient features of the amendments made to the SEBI ICDR concerning the KPIs are briefly discussed in the following paragraphs.

1. *Amendment to Schedule VI of the SEBI ICDR*: The fourth amendment has added two new sub-paras namely
  - ⊙ Sub-para (3) (a) to (i) and
  - ⊙ Sub-para (4(f))
 under the head “(K) – Basis for Issue Price” in Part-A (dealing with disclosures in offer document / letter of offer) of Schedule VI to the SEBI ICDR.
2. *Applicability*: It has been provided in the amendment notification that the new provisions shall apply for all Red Herring prospectus (RHP) filed on or after the effective date namely 21<sup>st</sup> November 2022.
3. *KPIs to be defined consistently and precisely [sub-para 3(a)]*: The Regulations require that the KPIs are defined consistently and precisely. These shall be disclosed by the issuer in the offer document. The emphasis of the Regulations is on the usage of simple English words, terms, and phrases for the definition of

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KPIs. Further, where technical terms are required to be used in explaining the KPIs, appropriate clarifications shall be given in such a manner that they are simple and easy to understand from an investor's perspective.

4. *Audit Committee approval [sub-para 3(b)]*: The Audit Committee shall approve the KPIs disclosed in the offer document of the issuer.
5. *Certification of the KPIs [sub-para 3(c)]*: Issuer shall obtain certification of the KPIs from one of the following professionals: -
  - ⊙ Statutory auditors of the company or individual CAs or a firm of CAs holding a valid peer review certificate or
  - ⊙ CMAs holding a valid peer review certificate.
 It is understood that the Institute of Cost Accountants of India is in the process of setting up the requisite peer review mechanism.
6. *Certificate to be included in the material documents [sub-para 3(d)]*: The certificate referred to in sub-para (3)(c) shall form part of the material documents listed in the offer document.
7. *Period for the KPIs [sub-para 3(e)]*: The period for which the KPIs are disclosed in the offer document shall be co-terminus with the period in respect of which financial statements are disclosed in the offer document.

In this connection, it may be noted that audited consolidated financial statements prepared in accordance with IND-AS for three full years and the stub period (part of the year), where applicable shall be included in the offer document. Thus, the KPIs that are disclosed in the offer document should be aligned with the periods covered by the CFS. It should also be remembered that the end of the stub period shall not be older by more than six months.

Further, a question has been raised as to whether the KPIs should also be disclosed on a consolidated basis. While there is no clear guideline on this point as yet, it appears that KPIs have to be disclosed on a consolidated basis if that is the manner in which the management of the Issuer has been historically analysing, tracking or monitoring the operational / financial performance of the company, as provided in the following sub-para (3)(f).

8. *Comprehensive [sub-para 3(f)]*: The Regulations provide that the KPIs that are disclosed in the offer document should be comprehensive. It is also provided that there should be explanation as to how the KPIs have been used by the management for historically analysing, tracking or monitoring both the operational and financial performance of the issuer company.
9. *Additions or Dispositions to Business and Comparison over time [sub-para 3(g)]*: The Regulations provide that when KPIs are compared over a period of time, adjustments shall be made for additions or dispositions to the business and explained. This is necessary from an investor point of view

for better understanding.

10. *Disclosures under the “Basis for Issue Price Section” [Sub-para 3(h)]*

- a. *Period of Disclosure [sub-para 3(h)(1)]:* The issuer company shall disclose all the KPIs that have been disclosed or shared with the investors during a period of 3 years before the date of filing of draft Red Herring prospectus (DRHP) / Red Herring prospectus (RHP). Further, in view of sub-para (3) (e) discussed above, such disclosure of KPIs should be co-terminus with the period of disclosure of the audited financial statements.
- b. *Confirmation by Audit Committee [sub-para 3(h)(2)]:* The issuer company shall obtain confirmation from the Audit Committee that they have “verified and audited” the details for all the KPIs that have been disclosed by the issuer company to the investors during the three years before the filing of DRHP / RHP. The offer document shall contain this confirmation.
- c. *Disclosure of other relevant KPIs [sub-para (3)(h)(3)]:* It is open to the issuer company in consultation with the lead merchant banker to disclose other relevant and material KPIs of the business of the issuer company as may be reckoned to be apposite for the purpose of arriving at the basis for issue price.
- d. *Cross Referencing of the KPIs [sub-para (3)(h)(4)]:* In case the issuer company has disclosed KPIs in other sections of

the offer document, they may be cross referenced in the “Basis for Issue Price” section of the offer document.

- e. *Comparison with listed peer companies [sub-para(h)(5)]:* Wherever available, the issuer company shall disclose the comparative KPIs of the listed peer companies (Indian or Global) as identified.

The identified peer companies shall be -

- ⊙ comparable in terms of size
- ⊙ belonging to the same industry and
- ⊙ operating on a similar business model.

In case the identified peer companies are not strictly comparable, suitable notes may be added to explain the differences.

11. *Continual Disclosures [sub-para(3)(i)]:* Issuer companies shall continue to disclose the KPIs forming part of the offer document on a periodic basis, the frequency of which shall be at least once in a year or a period of lesser frequency as may be decided by the issuer company.

The minimum duration during which the disclosures shall be continued to be made is specified as:

- a. one year after the listing date or such a period as specified by SEBI or
- b. until the utilisation of the issue proceeds for the objects of the issue as disclosed in the offer document

It is further provided that if there are any changes in the KPIs during the continuing period, the issuer company

shall provide explanation.

It is also provided that a Chartered Accountant or Cost Accountant referred to in sub-para (3)(c) shall certify the ongoing KPIs covered herein.

12. *Recommendation of a Committee of Independent Directors [sub-para (4)(f)]:* The recommendation of a Committee of Independent Directors of the issuer company with regard to the justification of the price band in the price band advertisement shall contain a reference of the justification based on quantitative factors and KPIs disclosed in the offer document in the “Basis for Issue Price” section vis-à-vis the weighted average cost of acquisition (WACA) of the primary issue / secondary transaction disclosed in the said section.

## WAY FORWARD

*“Not everything that can be counted counts and not everything that counts can be counted” -*

**-Albert Einstein**

Now that it has been recognised that KPIs are the driving force in the form of important inputs to the strategic management process, the regulatory prescription by SEBI requiring the issuers to disclose the KPIs in the offer document goes a long way in helping institutional investors in the primary market to take well informed decisions with respect to subscribing to public offers. How far it would impact the response of the retail investor, however, remains to be seen. In any case, the new Regulations have given the professionals including CMAs who have got through this recognition a new avenue for professional practice. It is now up to the CMAs to grab this opportunity and demonstrate their prowess through achieving excellence in this new area of professional opportunity. **MA**