Chapter: 4

Issue management: Discussion on SEBI Rules and Regulations

4.1 Prologue

As evident, the capital market primarily deals with long-term funds, which flow into the capital markets in various forms, come from various participants including individual investors, domestic financial institutions and foreign institutional investors (FIIs). Capital market provides a market mechanism for those who need funds for productive investments and also for those who want to make the most efficient utilization of their idle money. As we know, that it is a two-tier market comprising primary market and secondary market. A company in order to raise funds from public used to make it through primary market. The management of public issue has essentially become an exercise involving active participation of a number of agencies. A promoter as a principal representative of a company which is making the public issue should be clear about the number of agencies involved and their respective roles in the entire exercise.

In this segment, we will explore the rules and regulations framed by the SEBI for smooth functioning of the capital market and in protecting the interest of the investors as well. The detail rules and regulation on IPO and FPO have also been considered in detail here.

Moreover, various rules and regulations relating to issue management, pricing of issue, offer document and its content, categories of investor, role of SEBI in issue management, book building methods, fixed price method etc. are also considered here. SEBI guidelines on various other areas which have a ramification on IPO issue management will be explored such as IPO grading, classification of investors’ etc in the next few lines.

4.2 Philosophy of Regulation

The capital market is very much depended upon credibility and fairness of the participants. A sound regulatory framework is expected to provide transparency, maintain market integrity and fairness, and ensure investor protection through
awareness. There is no consensus amongst the expert as to what should be the right approach regarding the regulations of the market. One school of thought believes that markets are inherently efficient and over regulations lead to inefficiency in the functioning of the market. Consequently, this school of thought favours for minimal or no regulations. However, it is now seen that lack of adequate regulations can invite manipulations and market abuse by shrewd market players, which not only endangers market integrity but also damage investors’ confidence.

Therefore, to ensure transparency the role of regulatory body such as SEBI is essential for every facet of primary and secondary market activities and processes, fairness in the market is essential for efficient price discovery, which in turn leads to greater participation of investors. Another important job done through regulation is that it helps in reducing the systematic risk in the market.

Therefore, the perception of sound regulation is as important as the reality of regulation. To conclude, it is essential that the investor’s faith and confidence should persist and to ensure that the transparency of the market is maintained. The existence of strong regulatory body is of immense importance.

According to the preamble of the SEBI Act, 1992, the major objectives of SEBI are as follows:

1) To protect the interests of the investors in securities.
2) To promote the development of securities markets in India.
3) To regulate the securities market by stressing on the compliance of the norms issued by the organization.

In fact, the SEBI was established in the year 1988 to regulate and develop the growth of the capital market. It regulates the working of stock exchanges and intermediaries, accords approval of mutual funds, register FIIs who wish to participate in Indian stock market either through the route of equity or debt.
4.3 The placement of issues: A brief discussion

A company desirous to raise money from public may take the following routes of issue.

![Exhibit 4.1](image)

Let us briefly discuss the various forms of equity issues that exist in Indian capital market.

1. **Public issue**

This method of issuing shares is the most popular mode of raising share capital. Public issue method of raising capital involves raising of funds direct from the public, through primary market. More specifically we can call an issue as public when an issue or offer of securities is made to new investors for becoming a part of shareholders’ family of the issuers.

Public issue can further be classified into Initial Public offer (IPO) and Follow on or further Public Offer (FPO). The significant features of each type can briefly be described below:-
(a) **Initial Public Offer (IPO)**

When an unlisted company makes either a fresh issue of securities or offers, its existing securities for sale or both for the first time to the public, it is called an IPO. This paves the way for listing and subsequent trading of the securities in the stock exchange. As can be seen from the exhibit 4.1 above, SEBI has segregated the IPO into two sections i.e. fresh issue and offer for sale. Fresh issue means that the company is issuing the shares for the first time and the company in question, is used to be a private limited company and expectedly, no scrip’s were listed earlier in true sense of the term. This can be construed as the original version of IPO. While in case of offer for sale, the present owner dilutes his share of holding by selling his portion of shares. In this regard, it is to be noted that the shares under offer for sale are already listed in a bourse. Therefore, an IPO is a transformational event for an organization.

(b) **Follow on or Further Public offer (FPO):**

When an already listed company makes either a fresh issue of securities to the public or an offer for sale to the public, it is called as FPO. Like IPO it can be segregated into two parts one is for fresh issue and the other is known as offer for sale, the meaning of this terminology is same as in IPO.

2. **Rights Issue**

Under this method of issue, additional share capital is raised from the existing shareholders by offering securities to them on pre-emptive basis. The rights are offered in a particular ratio to the number of securities already held on a particular date fixed by the issuer (record date).

3. **Bonus issue**

When an issuer makes an issue of securities to its existing shareholders as on a record date, without any consideration from them, it is called a bonus issue. Bonus shares are distributed free of cost to the existing shareholders in a certain ratio. When a company accumulates sufficient profits or reserves to declare additional dividend but does not want additional outflow of cash, it may issue bonus shares by conversion of retained profits or reserves into equity share capital.
4. Private placement

When an issuer makes an issue of securities to a select group of persons not exceeding 49%, and which is neither rights issue nor a public issue, it is called a private placement. It is estimated that in a public issue, 10% of the proceeds are used as issue related expenditure and in that sense this method seems obviously cost effective. Arrangements of public issue will take a lot of time while within a short period, the company can raise its target amount from the market through private placement. Private placement of shares or convertible securities by listed issuer can be of two types.

(a) Preferential allotment

When a listed issuer issues shares or convertible to securities, to a select group of persons in terms of provisions of Chapter XIII of SEBI (DIP) guidelines, it is called a preferential allotment. The issuer is required to comply with various provisions which inter-alia includes pricing, disclosures etc. and is specified in the Companies Act.

(b) Qualified Institutional Placement

When a listed company issues equity shares or securities convertible into equity shares to Qualified Institutional Buyers only in terms of provisions of Chapter XIII A of SEBI (DIP) guidelines it is called a QIP.

4.4 Rules governing Issue of Capital in Indian Market

In order to raise funds via equity route, due regard has to be given to the following Acts, Rules, Regulations and Guidelines.

I. Provisions of the Companies Act, 1956

II. SEBI Guidelines and Clarifications

III. The Securities Contracts (Regulation) Act, 1956

IV. The Securities Contracts (Regulations) Rules, 1957

Thus, the above rules, regulations and guidelines are the basic rules or Acts that a company must adhere to while issuing equity shares in India. However, it should be remembered that besides this provision or Acts, there are other aspects also in respect to issue of equity shares. As we are well aware that the managing of the
capital markets and its various activities are governed by the union ministry and the 
nature or the field of activity of the company is also being governed by a particular 
ministry, so it is important that the respective company must comply with the rules 
before and after the issue.

In India, the role of SEBI as guardian of capital market is widely acclaimed 
and recognized. However, the following list of regulatory bodies sometimes makes 
the matter even more stringent. This list shows that the regulatory body goes on 
changing with the type of organization and sometimes there are multiple 
organizations governing a particular sector or area. The following table gives us a 
fairly good idea about the various organizations and ministry which regulate the 
various matter related to public issue in the capital market.

Table 4.1
Role of SEBI vis-à-vis other regulators

<table>
<thead>
<tr>
<th>Type of Entity</th>
<th>Regulatory body</th>
</tr>
</thead>
<tbody>
<tr>
<td>Auditors</td>
<td>ICAI/CAG</td>
</tr>
<tr>
<td>Banks</td>
<td>RBI</td>
</tr>
<tr>
<td>Banks - Issue Collection</td>
<td>SEBI</td>
</tr>
<tr>
<td>Chit Funds</td>
<td>REGISTRAR OF CHIT FUNDS</td>
</tr>
<tr>
<td>Collective Investment Schemes</td>
<td>SEBI</td>
</tr>
<tr>
<td>Companies – All</td>
<td>MCA/ROC</td>
</tr>
<tr>
<td>Companies – Listed</td>
<td>MCA/ROC/SEBI</td>
</tr>
<tr>
<td>Credit Rating Agencies</td>
<td>SEBI</td>
</tr>
<tr>
<td>Custodial Services</td>
<td>SEBI</td>
</tr>
<tr>
<td>Debenture Trustees</td>
<td>SEBI</td>
</tr>
<tr>
<td>Depositories</td>
<td>SEBI</td>
</tr>
<tr>
<td>Depository Participants</td>
<td>SEBI/NSDL/CDSL</td>
</tr>
<tr>
<td>Financial Institutions</td>
<td>MOF</td>
</tr>
<tr>
<td>Foreign Brokers</td>
<td>SEBI</td>
</tr>
<tr>
<td>Foreign Debt Funds</td>
<td>SEBI</td>
</tr>
<tr>
<td>Foreign Investment Institutions</td>
<td>SEBI</td>
</tr>
<tr>
<td>Insurance Companies</td>
<td>IRDA</td>
</tr>
<tr>
<td>Investor Associations</td>
<td>SEBI</td>
</tr>
<tr>
<td>Mutual Funds &amp; Asset Management Companies</td>
<td>SEBI</td>
</tr>
<tr>
<td>Mutual Fund Brokers/ Agents</td>
<td>AMFI/SEBI</td>
</tr>
<tr>
<td>Non-Banking Financial Companies (NBFCs)</td>
<td>RBI</td>
</tr>
<tr>
<td>Nidhi Companies</td>
<td>MCA</td>
</tr>
<tr>
<td>Primary Dealers</td>
<td>RBI</td>
</tr>
<tr>
<td>Registrars &amp; Share Transfer Agents</td>
<td>SEBI</td>
</tr>
<tr>
<td>Stock Brokers</td>
<td>SEBI/SE</td>
</tr>
<tr>
<td>Stock Exchanges</td>
<td>SEBI</td>
</tr>
<tr>
<td>Sub-Brokers</td>
<td>SEBI</td>
</tr>
<tr>
<td>TV Channels</td>
<td>MIB</td>
</tr>
</tbody>
</table>

Source: Investors guide to investment, Prithvi Haldea (2010)
The Securities Contracts (Regulations) Rules, 1957 (SCRR) dealt with the listing and trading of securities on stock exchanges. The same have been amended from time to time to respond to changing needs of securities market. One of the major amendments in the realm of SCR Rules happened in 2010.

**SCR-Rule 19(2) (b) - prior to 4.6.2010**

Rule 19(2) (b) provides that a company can get listed with just 10 percent holding with the public provided the minimum net offer to the public is Rs100 crore (Rs. 1 billion), a minimum of 20 lakh (2 million) net offer to the public in an IPO through book building method and allocation to qualified institutional buyers is 60% the size of issue.

**SCR- Amendment dated 4.6.2010**

Following are the latest amendments made in the realm of public issue especially, in case of IPO.

(a) The minimum threshold level of public holding will be 25% for all the listed companies.

(b) Existing listed companies having less than 25% public holding have to reach the minimum 25% level by an annual addition of not less than 5% to public holding.

(c) For newly listed companies, if the post-issue capital of the company calculated at offer price is more than Rs. 4000 crore, the company may be allowed to go public with 10% public shareholding and comply with the 25% public shareholding requirement by increasing its public shareholding by at least 5% per annum.

(d) For companies whose draft offer document is pending with SEBI on or before these amendments are required to comply with 25% public shareholding requirements by increasing its public shareholding by at least 5% per annum, irrespective of the amount of past issue capital of the company calculated at offer price.
(e) A company may increase its public shareholding by less than 5% in a year if such increase brings its public shareholding to the level of 25% in that year.

(f) The requirement for continuous listing will be the same as the conditions for initial listing.

(g) Every listed company shall maintain public shareholding of at least 25%. If the public shareholding in a listed company falls below 25% at any time, such company shall bring the public shareholding to 25% within a maximum period of 12 months from the date of such fall.

4.5 Eligibility criteria for Public Issue

As prescribed by SEBI Regulation 2009, unless otherwise provided, an issuer making a public issue shall satisfy the conditions of certain provision as on the date of filing draft offer documents with the Board and also as on the date of registering the offer documents with the Registrar of Companies (ROCs).

Conditions for initial public offer

(1) An issuer may make an initial public offer, if:

(a) it has net tangible assets of at least three crore rupees in each of the preceding three full years (of twelve months each), of which not more than fifty per cent are held in monetary assets: [Provided that if more than fifty per cent of the net tangible assets are held in monetary assets, the issuer has made firm commitments to utilise such excess monetary assets in its business or project;]

(b) it has a track record of distributable profits in terms of section 205 of the Companies Act, 1956, for at least three out of the immediately preceding five years; provided that extraordinary items shall not be considered for calculating distributable profits;

(c) it has a net worth of at least one crore rupees in each of the preceding three full years (of twelve months each);

(d) the aggregate of the proposed issue and all previous issues made in the same financial year in terms of issue size does not exceed five times of its
pre-issue net worth as per the audited balance sheet of the preceding financial year;

(e) if it has changed its name within the last one year, at least fifty per cent of the revenue for the preceding one full year has been earned by it from the activity indicated by the new name.

(2) An issuer not satisfying any of the conditions stipulated in sub-regulation (1) may make an initial public offer if:

(a) (i) the issue is made through the book building process and the issuer undertakes to allot at least fifty per cent of the net offer to public, qualified institutional buyers and to refund full subscription monies if it fails to make allotment to the qualified institutional buyers;

or

(ii) at least fifteen per cent of the cost of the project is contributed by scheduled commercial banks or public financial institutions, of which not less than ten per cent shall come from the appraisers and the issuer undertakes to allot at least ten per cent of the net offer to public, to qualified institutional buyers and to refund full subscription monies if it fails to make the allotment to the qualified institutional buyers;

(b) (i) the minimum post-issue face value capital of the issuer is ten crore rupees;

or

(ii) the issuer undertakes to provide market-making for at least two years from the date of listing of the specified securities, subject to the following:

A. the market makers offer buy and sell quotes for a minimum depth of three hundred specified securities and ensure that the bid-ask spread for their quotes does not, at any time, exceed ten per cent;

B. The inventory of the market makers, as on the date of allotment of the specified securities, shall be at least five per cent of the proposed issue.

(3) An issuer may make an initial public offer of convertible debt instruments without making a prior public issue of its equity shares and listing thereof.
(4) An issuer shall not make an allotment pursuant to a public issue if the number of prospective allottees is less than one thousand.

(5) No issuer shall make an initial public offer if there are any outstanding convertible securities or any other right which would entitle any person option to receive equity shares after the initial public offer:

Provided that the provisions of this sub-regulation shall not apply to:

(a) a public issue made during the currency of convertible debt instruments which were issued through an earlier initial public offer, if the conversion price of such convertible debt instruments was determined and disclosed in the prospectus of the earlier issue of convertible debt instruments;

(b) outstanding options granted to employees pursuant to an employee stock option scheme framed in accordance with the relevant Guidance Note or Accounting Standards, if any, issued by the Institute of Chartered Accountants of India in this regard.

(6) Subject to provisions of the Companies Act, 1956 and these regulations, equity shares may be offered for sale to public if such equity shares have been held by the sellers for a period of at least one year prior to the filing of draft offer document with the Board in accordance with sub-regulation (1) of regulation 6:

[Provided that in case of equity shares received on conversion or exchange of fully paid-up compulsorily convertible securities including depository receipts are being offered for sale, the holding period of such convertible securities as well as that of resultant equity shares together shall be considered for the purpose of calculation of one year period referred in this sub-regulation:]

Provided further that the requirement of holding equity shares for a period of one year shall not apply:

(a) in case of an offer for sale of specified securities of a government company or statutory authority or corporation or any special purpose vehicle set up and controlled by any one or more of them, which is engaged in infrastructure sector;
(b) if the specified securities offered for sale were acquired pursuant to any scheme approved by a High Court under sections 391-394 of the Companies Act, 1956, in lieu of business and invested capital which had been in existence for a period of more than one year prior to such approval.

(7) No issuer shall make an initial public offer, unless as on the date of registering prospectus or red herring prospectus with the Registrar of Companies, the issuer has obtained grading for the initial public offer from at least one credit rating agency registered with the Board.

**Explanation:** For the purposes of this regulation: following explanations are being provided by the SEBI:

(I) “net tangible assets” mean the sum of all net assets of the issuer, excluding intangible assets as defined in Accounting Standard 26 (AS 26) issued by the Institute of Chartered Accountants of India;

(II) “project” means the object for which monies are proposed to be raised to cover the objects of the issue;

(III) in case of an issuer which had been a partnership firm, the track record of distributable profits of the partnership firm shall be considered only if the financial statements of the partnership business for the period during which the issuer was a partnership firm, conform to and are revised in the format prescribed for companies under the Companies Act, 1956 and also comply with the following:

(a) adequate disclosures are made in the financial statements as required to be made by the issuer as per Schedule VI of the Companies Act, 1956;

(b) the financial statements are duly certified by a Chartered Accountant stating that:

- accounts and the disclosures made are in accordance with the provisions of Schedule VI of the Companies Act, 1956;
- the accounting standards of the Institute of Chartered Accountants of India have been followed;
- The financial statements present a true and fair view of the firm’s accounts.
(IV) In case of an issuer formed out of a division of an existing company, the track record of distributable profits of the division spun-off shall be considered only if the requirements regarding financial statements as provided for partnership firms in Explanation III are complied with;

(V) “Bid-ask spread” means the difference between quotations for sale and purchase;

(VI) The term “infrastructure sector” includes the facilities or services as specified in Schedule X.

Conditions for further public offer

An issuer may make a further public offer if it satisfies the conditions specified in clauses (d) and (e) of sub-regulation (1) of regulation 26 and if it does not satisfy those conditions, it may make a further public offer if it satisfies the conditions specified in sub-regulation (2) of regulation.

Offer Documents (ODs)

It is a document which contains all the relevant information about the company, promoters, projects, financial details, objects of raising the money, terms of the issue etc and is used for inviting subscription to the issue being made by the issuer. ‘Offer Document’ is called “Prospectus” in case of a public issue or offer for sale and “Letter of Offer” in case of a rights issue.

We come across with the various terms used for offer documents depending upon the stage or type of the issue where the document is used. The terms used for offer documents are defined by SEBI as below:

(i) **Draft offer document** is an offer document filed with SEBI for specifying changes, if any, in it, before it is filed with the ROC. Draft offer document is made available in public domain including SEBI website, for enabling public to give comments, if any, on the draft offer document.

(ii) **Red herring prospectus** is an offer document used in case of a book built public issue. It contains all the relevant details except that of price or number of shares being offered. It is filled with RoC before the issue opens.
(iii) **Prospectus** is an offer document in case of a public issue, which has all relevant details including price and number of shares being offered. This document is registered with RoC before the issue opens in case of a fixed price offer and after the closure of the issue in case of a book built issue.

(iv) **Letter of offer** is an offer document in case of a rights issue and is filed with stock exchanges before the issue opens.

(v) **Abridged prospectus** is an abridged version of offer document in public issue and is issued along with the application form of a public issue. It contains all the salient features of a prospectus.

(vi) **Abridged letter of offer** is an abridged version of the letter of offer. It is sent to all the shareholders along with the application form.

(vii) **Shelf prospectus** is a prospectus which enables an issuer to make a series of issues within a period of 1 year without the need of filing a fresh prospectus every time. This facility is available to public sector banks /Public Financial Institutions.

(viii) **Placement document** is an offer document for the purpose of Qualified Institutional Placement and contains all the relevant and material disclosures.

### 4.6 Fast Track Issues (FTI): Rules and Guidelines

SEBI has introduced FTI in order to enable well established and compliant listed companies satisfying certain specific entry norms/conditions to access Indian primary market in a time effective manner. Such companies can proceed with FPOs / right issues by filing a copy of RHP / Prospectus with the ROC or the letter of offer with designated SE, SEBI and stock exchanges. Such companies are not required to file draft offer document for SEBI comments and to stock exchanges.

Entry norms for companies seeking access to primary market through FTI’s in case aggregate value of securities including premium exceeds Rs. 50 lacs:

(i) The shares of the company have been listed on any stock exchange having nationwide terminals for a period of at least three years immediately preceding the date of filing of offer document with RoC/ SE.
(ii) The “average market capitalisation of public shareholding” of the company is at least Rs. 10,000 crores for a period of one year up to the end of the quarter preceding the month in which the proposed issue is approved by the Board of Directors / shareholders of the issuer.

(iii) The annualized trading turnover of the shares of the company during six calendar months immediately preceding the month of the reference date has been at least two percent of the weighted average number of shares listed during the said six months period.

(iv) The company has redressed at least 95% of the total shareholder / investor grievances or complaints received till the end of the quarter immediately preceding the month of the date of filing of offer document with ROC/ SE.

(v) The company has complied with the listing agreement for a period of at least three years immediately preceding the reference date.

(vi) The impact of auditors’ qualifications, if any, on the audited accounts of the company in respect of the financial years for which such accounts are disclosed in the offer document does not exceed 5% of the net profit/ loss after tax of the company for the respective years.

(vii) No prosecution proceedings or show cause notices issued by the Board are pending against the company or its promoters or whole time directors as on the reference date. and

(viii) The entire shareholding of the promoter group is held in dematerialised form as on the reference date.

**Opening of an issue**

(1) Subject to the compliance with sub-section (4) of section 60 of the Companies Act, 1956, a public issue or rights issue may be opened:

(a) within twelve months from the date of issuance of the observations by the Board under regulation 6; or

(b) within three months of expiry of the period stipulated in sub-regulation (2) of regulation 6, if the Board has not issued observations: *Provided that in case of a fast track issue, the issue shall open within the period stipulated*
(2) In case of shelf prospectus, the first issue may be opened within three months of issuance of observations by the Board.

(3) The issuer shall, before registering the red herring prospectus (in case of a book built issue) or prospectus (in case of a fixed price issue) with the Registrar of Companies or filing the letter of offer with the designated stock exchange, as the case may be, file with the Board through the lead merchant bankers, an updated offer document highlighting all changes made in the offer document.

(4) Notwithstanding anything contained in this regulation, if there are changes in the offer document in relation to the matters specified in Schedule VII, the updated offer document or new draft offer document, as the case may be, shall be filed with the Board along with requisite fees specified in Schedule IV.

**Underwriting**

(1) Where the issuer making a public issue (other than through the book building process) or rights issue, desires to have the issue underwritten, it shall appoint the underwriters in accordance with Securities and Exchange Board of India (Underwriters) Regulations, 1993.

(2) Where the issuer makes a public issue through the book building process, such issue shall be underwritten by book runners or syndicate members:

[Provided that fifty per cent [sixty per cent, if public issue is made with at least ten per cent public offer under clause (b) of sub-rule (2) of rule 19 of the Securities Contracts (Regulation) Rules, 1957] of the net offer to public proposed to be compulsorily allotted to qualified institutional buyers for the purpose of compliance of the eligibility conditions specified in sub-regulation (2) of regulation 26 and regulation 28 cannot be underwritten.]

(3) The issuer shall enter into underwriting agreement with the book runner, who in turn shall enter into underwriting agreement with syndicate members, indicating therein the number of specified securities which they shall subscribe to at the predetermined price in the event of under-subscription in the issue.
(4) If syndicate members fail to fulfill their underwriting obligations, the lead
book runner shall fulfill the underwriting obligations.

(5) The book runners and syndicate members shall not subscribe to the issue in
any manner except for fulfilling their underwriting obligations.

(6) A copy of the syndicate agreement shall be filed with the Board before the
opening of bids.

(7) In case of every underwritten issue, the lead merchant banker or the lead book
runner shall undertake minimum underwriting obligations as specified in the
Securities and Exchange Board of India (Merchant Bankers) Regulations,

(8) Where hundred per cent of the offer through offer document is underwritten,
the underwriting obligations shall be for the entire hundred per cent of the
offer through offer document and shall not be restricted up to the minimum
subscription level.

**Minimum subscription**

(1) The minimum subscription to be received in an issue shall not be less than
ninety per cent of the offer through offer document.

(2) In the event of non-receipt of minimum subscription referred to in sub-
regulation (1), all application moneys received shall be refunded to the
applicants forthwith, but not later than:

(a) fifteen days of the closure of the issue, in case of a non-underwritten issue;
and

(b) seventy days of the closure of the issue, in the case of an underwritten
issue where minimum subscription including devolvement obligations paid
by the underwriters is not received within sixty days of the closure of the
issue.

(3) The offer document shall contain adequate disclosures regarding minimum
subscription as specified in **Part A of Schedule VIII**.

(4) Nothing contained in this regulation shall apply to:
(a) offer for sale of specified securities;

(b) public issue by infrastructure companies if the disclosures regarding the alternate source of funding of the objects of the issue have been made in the offer document.

**Explanation:** [For the purpose of clause (b) of sub-regulation (4), the term “infrastructure company” means, an enterprise wholly engaged in the business of (i) developing or (ii) operating and maintaining or (iii) developing, operating and maintaining any infrastructure facility.]

**Oversubscription**

No allotment shall be made by the issuer in excess of the specified securities offered through the offer document:

[Provided that in case of oversubscription, an allotment of not more than ten per cent. of the net offer to public may be made for the purpose of making allotment in minimum lots.]

**Monitoring agency**

(1) If the issue size exceeds five hundred crore rupees, the issuer shall make arrangements for the use of proceeds of the issue to be monitored by a public financial institution or by one of the scheduled commercial banks named in the offer document as bankers of the issuer:

[Provided that nothing contained in this clause shall apply to an offer for sale or an issue of specified securities made by a bank or public financial institution.]

(2) The monitoring agency shall submit its report to the issuer in the format specified in **Schedule IX** on a half yearly basis, till the proceeds of the issue have been fully utilised.

**Manner of calls**

If the issuer proposes to receive subscription monies in calls, it shall ensure that the outstanding subscription money is called within twelve months from the date
of allotment in the issue and if any applicant fails to pay the call money within the said twelve months, the equity shares on which there are calls in arrear along with the subscription money already paid on such shares shall be forfeited.

[Provided that it shall not be necessary to call the outstanding subscription money within twelve months, if the issuer has appointed a monitoring agency in terms of regulation 16.]

Allotment, refund and payment of interest

(1) The issuer and merchant bankers shall ensure that specified securities are allotted and/or application moneys are refunded within fifteen days from the date of closure of the issue.

(2) Where specified securities are not allotted and/or application moneys are not refunded within the period stipulated in sub-regulation (1), the issuer shall undertake to pay interest at such rate and within such time as disclosed in the offer document.

Restriction on further capital issues

No issuer shall make any further issue of specified securities in any manner whether by way of public issue, rights issue, preferential issue, qualified institutions placement, issue of bonus shares or otherwise:

(a) in case of a fast track issue, during the period between the date of registering the red herring prospectus (in case of a book built issue) or prospectus (in case of a fixed price issue) with the Registrar of Companies or filing the letter of offer with the designated stock exchange and the listing of the specified securities offered through the offer document or refund of application moneys.

or

(b) in case of other issues, during the period between the date of filing the draft offer document with the Board and the listing of the specified securities offered through the offer document or refund of application moneys.

Unless full disclosures regarding the total number of specified securities and
amount proposed to be raised from such further issue are made in such draft offer
document or offer document, as the case may be.

4.7 Some relevant factors involved in IPO issues

In this section we will delineate certain players who are involved either
directly or indirectly with the process of IPO issue such as the various intermediaries
who act as liaison between the issuing firm and the most important player of the entire
episode, the investors.

4.7.1 Intermediaries and their role in the Issue Process

Intermediaries which are registered with SEBI are merchant bankers to the
issue (known as book running lead managers (BRLM) in case of book built public
issues), registrars to the issue and bankers to the issue & underwriters to the issue who
are associated with the issue for different activities. Their addresses, telephone/fax
numbers, registration number, and contact person and email addresses are disclosed in
the offer documents.

(i) Merchant Banker

Merchant banker does the due diligence to prepare the offer document which
contains all the details about the company. They are also responsible for
ensuring compliance with the legal formalities in the entire issue process and
for marketing of the issue.

(ii) Registrars to the Issue

They are involved in finalizing the basis of allotment in an issue and for
sending refunds, allotment etc.

(iii) Bankers to the Issue

The Bankers to the Issue enable the movement of funds in the issue process
and therefore enable the registrars to finalize the basis of allotment by making
clear funds status available to the Registrars.

(iv) Underwriters

Underwriters are intermediaries who undertake to subscribe to the securities
offered by the company in case these are not fully subscribed by the public, in
Documents to be submitted before opening of the issue

(1) The lead merchant bankers shall submit the following to the Board along with the draft offer document:

(a) a copy of the agreement entered into between the issuer and the lead merchant bankers.

(b) a copy of inter-se allocation of responsibilities of each merchant banker, in case the issue is managed by more than one merchant banker.

(c) a due diligence certificate as per Form A of Schedule VI;

(d) in case of an issue of convertible debt instruments, a due diligence certificate from the debenture trustee as per Form B of Schedule VI;

(e) a certificate in the format specified in Part D of Schedule VII, confirming compliance of the conditions mentioned therein.

(2) The lead merchant bankers shall submit the following documents to the Board after issuance of observations by the Board or after expiry of the period stipulated in sub-regulation (2) of regulation 6 if the Board has not issued observations:

A statement certifying that all changes, suggestions and observations made by the Board

(a) have been incorporated in the offer document.

(b) a due diligence certificate as per Form C of Schedule VI, at the time of registering the prospectus with the ROC.

(c) a copy of the resolution passed by the board of directors of the issuer for allotting specified securities to promoters towards amount received against promoters’ contribution, before opening of the issue.

(d) a certificate from a Chartered Accountant, before opening of the issue, certifying that promoters’ contribution has been received in accordance with these regulations, accompanying therewith the names and addresses of the promoters who have contributed to the promoters’ contribution and
the amount paid by each of them towards such contribution.

(e) a due diligence certificate as per Form D of Schedule VI, immediately before the opening of the issue, certifying that necessary corrective action, if any, has been taken.

(3) The issuer shall, at the time of filing draft offer document with the recognised stock exchange where the specified securities are proposed to be listed, submit the Permanent Account Number, bank account number and passport number of its promoters to such stock exchange.

**Draft offer document to be made public**

(1) The draft offer document filed with the Board shall be made public, for comments, if any, for a period of at least twenty one days from the date of such filing, by hosting it on the websites of the Board, recognised stock exchanges where specified securities are proposed to be listed and merchant bankers associated with the issue.

(2) The lead merchant bankers shall, after expiry of the period stipulated in sub-regulation (1), file with the Board a statement giving information of the comments received by them or the issuer on the draft offer document during that period and the consequential changes, if any, to be made in the draft offer document.

**Appointment of merchant banker and other intermediaries**

(1) The issuer shall appoint one or more merchant bankers, at least one of whom shall be a lead merchant banker and shall also appoint other intermediaries, in consultation with the lead merchant banker, to carry out the obligations relating to the issue.

(2) The issuer shall, in consultation with the lead merchant banker, appoint only those intermediaries which are registered with the Board.

(3) Where the issue is managed by more than one merchant banker, the rights, obligations and responsibilities, relating inter alia to disclosures, allotment, refund and underwriting obligations, if any, of each merchant banker shall be predetermined and disclosed in the offer document as specified in Schedule I.
(4) The lead merchant banker shall, only after independently assessing the capability of other intermediaries to carry out their obligations, advise the issuer on their appointment.

(5) The issuer shall enter into an agreement with the lead merchant banker in the format specified in Schedule II and with other intermediaries as required under the respective regulations applicable to the intermediary concerned:

[Provided that such agreements may include such other clauses as the issuer and the intermediary may deem fit without diminishing or limiting in any way the liabilities and obligations of the merchant bankers, other intermediaries and the issuer under the Act, the Companies Act, 1956, the Securities Contracts (Regulation) Act, 1956, the Depositories Act, 1996 and the rules and regulations made hereunder or any statutory modification or statutory enactment thereof:]

[Provided further that in case of ASBA process, the issuer shall take cognizance of the deemed agreement of the issuer with Self Certified Syndicate Banks.]

(6) An issuer shall, in case of an issue made through the book building process, appoint syndicate members and in the case of any other issue, appoint bankers to issue, at all mandatory collection centers as specified in Schedule III and such other collection centers as it may deem fit.

(7) The issuer shall appoint a registrar which has connectivity with all the depositories:

[Provided that if issuer itself is a registrar to an issue registered with the Board, then another registrar to an issue shall be appointed as registrar to the issue:]

[Provided further that the lead merchant banker shall not act as a registrar to the issue in which it is also handling the post issue responsibilities.]

Explanation: For the purpose of this regulation, in case of a book built issue, the lead merchant banker appointed by the issuer shall act as the lead book runner.

Filing of offer document

(1) No issuer shall make,

(a) a public issue; or
(b) a rights issue,

Where the aggregate value of the specified securities offered is fifty lakh rupees or more, unless a draft offer document, along with fees as specified in Schedule IV, has been filed with the Board through the lead merchant banker, at least thirty days prior to registering the prospectus, red herring prospectus or shelf prospectus with the Registrar of Companies or filing the letter of offer with the designated stock exchange, as the case may be.

(2) The Board may specify changes or issue observations, if any, on the draft offer document within thirty days from the later of the following dates: The date of receipt of the draft offer document under sub-regulation (1);

or

(a) the date of receipt of satisfactory reply from the lead merchant bankers, where the Board has sought any clarification or additional information from them;

or

(b) the date of receipt of clarification or information from any regulator or agency, where the Board has sought any clarification or information from such regulator or agency;

or

(c) the date of receipt of a copy of in-principle approval letter issued by the recognised stock exchanges.

(3) If the Board specifies changes or issues observations on the draft offer document, the issuer and lead merchant banker shall carry out such changes in the draft offer document and comply with the observations issued by the Board before registering the prospectus, red-herring prospectus or shelf prospectus, as the case may be, with the ROC or filing the letter of offer with the designated stock exchange.

(4) The issuer shall, simultaneously while registering the prospectus, red herring prospectus or shelf prospectus with the ROC or filing the letter of offer with
the designated stock exchange or before the opening of the issue, file a copy thereof with the Board through the lead merchant banker.

(5) The lead merchant banker shall, while filing the offer document with the Board in terms of sub-regulation (1) and sub-regulation (4), file a copy of such document with the recognised stock exchanges where the specified securities are proposed to be listed.

(6) The offer document filed with the Board under this regulation shall also be furnished to the Board in a soft copy in the manner specified in Schedule V.

Exhibit 4.2
Intermediary Structure

Source: icsi.edu/docs/portals
The above figure exhibits the various intermediaries involved in the process of public issue along with their structure (including IPO) and how their function complement each other in order to make the process of new issue a successful endeavour. Let us briefly discuss some of the terminologies used in the above exhibit such as SCSB. It is the acronym of the word Self Certified Syndicate Bank (SCSB). It is a bank which offers the facility of applying through ASBA process. A bank desirous of offering ASBA facility shall submit a certificate to SEBI as per format given in Annexure I, for inclusion of its name in SEBI list of SCSBs. So an issuer company must engage with SCSB for the smooth functioning. From this figure, it is evident that for smooth functioning of IPO process the involvement of all the player of intermediaries are pre-requisite. The principal task of issue management is usually entrusted to the BRLM by the issuer company. The BRLM does the work of coordination among the various intermediaries involved in the issue process.

**Eligibility criteria of using ASBA:**

ASBA (Application Supported by Blocked Amount) is an application for subscribing to an issue, containing an authorization to block the application money in a bank account. An investor shall be deemed eligible to apply through ASBA process, if he/she:-

I. is a “Resident Retail Individual investors”

II. is bidding a cut-off, with single option as to the number of share bid for

III. is applying through blocking of funds, in a bank account with the SCSB

IV. has agreed not to revise his/her bid

V. is not bidding under any of the reserved categories.

**ASBA Process in brief:**

An ASBA investor shall submit an ASBA physically or electronically through the internet banking facility to the SCSB, with whom the bank account to be blocked, is maintained. The SCSB shall then block the application money in the bank account specified in the ASBA, on the basis of an authorisation to this effect given by the
account holder in the ASBA. The application money shall remain blocked in the bank account till finalisation on the basis of allotment in the issue or till withdrawal/ failure of the issue or till withdrawal/ rejection of the application, as the case may be. The application data shall, thereafter be uploaded by the SCSB in the electronic bidding system through a web enabled interface provided by the Stock Exchanges. Once the basis of allotment is finalized, the ROC shall send an appropriate request to the SCSB for unblocking the relevant bank accounts and for transferring the requisite amount to the issuer’s account. In case of withdrawal/ failure of the issue, the amount shall be unblocked by the SCSB on receipt of information from the pre-issue merchant bankers.

4.7.2 Categories of Investors in new issue

Investors are broadly classified under following categories:

(i) Retail Individual Investor (RIIs)

(ii) Non-Institutional Investors (NIIs)

(iii) Qualified Institutional Buyers (QIBs)

“Retail individual investor” means an investor who applies or bids for securities for a value of not more than Rs. 1,00,000. The market regulator SEBI has doubled the limit for retail investors from Rs. 1,00,000 to Rs. 2,00,000. The minimum application size for the retail investors has also been increased from existing Rs. 5,000-7,000 to Rs. 10,000-15,000.

“Qualified Institutional Buyer” shall mean:

(a) a public financial institution as defined in section 4A of the Companies Act, 1956

(b) a scheduled commercial bank

(c) a mutual fund registered with the Board

(d) a foreign institutional investor and sub-account registered with SEBI, other than a sub account which is a foreign corporate or foreign individual

(e) a multilateral and bilateral development financial institution
(f) a venture capital fund registered with SEBI

(g) a foreign venture capital investor registered with SEBI

(h) a state industrial development corporation.

(i) an insurance company registered with the Insurance Regulatory and Development Authority (IRDA)

(j) a provident fund with minimum corpus of Rs. 25 crores.

(k) a pension fund with minimum corpus of Rs. 25 crores.


Investors who do not fall within the definition of the above two categories are categorized as “Non-Institutional Investors”

A promoter group includes the following

As per the guidelines issued by the SEBI following group of people can be regarded as a promoter group

1. The promoter;

2. An immediate relative of the promoter; and

3. In case the promoter is a company:
   a) a subsidiary or holding company of that company;
   b) any company in which the promoter holds ten percent (10%) or more of the equity capital or which holds ten percent (10%) or more of the equity capital of the promoter.
   c) any company in which a group of individuals, companies or combinations thereof holds twenty percent (20%) or more of the equity capital and also holds twenty percent (20%) or more of the equity capital of the issuer company; and
4. In case the promoter is an individual:

   (a) any company in which the promoter, an immediate relative of the promoter or a firm in which the promoter or his immediate relative is a member, holds ten percent (10%) or more of the share capital.

   (b) any company in which a company specified in (a) above, holds ten percent (10%) or more, of the share capital, and

   (c) any firm in which the aggregate share of the promoter and his immediate relatives is equal to or more than ten percent (10%) of the total; and

5. All persons whose shareholding is aggregated for the purpose of disclosing in the prospectus as the shareholding of the promoter group.

   Financial institutions, scheduled banks, foreign institutional investors and mutual funds are not deemed to be a promoter or a promoter group merely because they hold ten percent (10%) or more of the equity of the issuer company. However, such entities will be treated as promoters or a promoter group with respect to the subsidiaries or companies promoted by them or for the mutual funds sponsored by them.

   The following will not be eligible to be considered for computation of the promoters’ contribution:

   1. Equity acquired by promoters of a company during the three (3) years preceding the filing of the offer document with the SEBI, if it:

      (a) is acquired for consideration other than cash and revaluation of assets or capitalization of intangible assets is involved in such transactions;

      or

      (b) Results from a bonus issue, out of revaluation of reserves, or reserves without accrual of cash resources (Clause 4.6.1 of the DIP Guidelines);

   2. Securities that have been issued to the promoters, during the preceding year, at a lower price than at which they are being offered to the public, except if the promoters bring in difference between the offer price and the issue price for the shares and all the requirements under the Companies Act, 1956 are
fulfilled, i.e., passing of revised by shareholders or Board filing of the revised return of allotment with the ROC, etc. (Clause 4.6.2 of the DIP Guidelines); and

3. Securities for which a specific written consent has not been obtained from the shareholders for inclusion of their shares in the minimum promoters’ contribution subject to lock-in. (Clause 4.6.7 of the DIP Guidelines)

4. The ineligible shares mentioned in 1 and 2 above, acquired in pursuant to a scheme of merger or amalgamation approved by a High Court, will be eligible to compute the promoters’ contribution. (Clause 4.6.4 of the DIP Guidelines)

5. A minimum contribution of Rs. 25,000 (Rupees twenty-five thousand) per application from each individual and Rs. 100,000 (Rupees hundred thousand) from firms and companies will be eligible for consideration to calculate the minimum promoters’ contribution. (Clause 4.6.5 of the DIP Guidelines)

6. The promoters must bring in the full amount of contribution at least one (1) day before the issue opening date, to be kept in an escrow account with a scheduled commercial bank, which will be released to the company along with the public issue proceeds. If the promoters’ contribution has been brought before the public issue and has already been deployed by the company, the company must give a cash flow statement in the offer document, disclosing how the promoters’ contribution was used. If the minimum promoters’ contribution exceeds Rs10,000,000 (Rupees ten million), the promoters must bring in Rs. 10,000,000 (Rupees ten million) before the opening of the issue and the remaining amount on a pro rata basis before the calls are made on the public (Clause 4.9.1 of the DIP Guidelines).

The company’s Board must pass a resolution allotting the shares or convertible instruments to the promoters against the amount received. A copy of the resolution and a certificate from a chartered accountant indicating receipt of the promoters’ contribution must be filed with the SEBI. A list of the names and addresses of friends, relatives and associates who have contributed to the promoters’ quota and their subscription amount must also be attached to the chartered accountant’s certificate. (Clause 4.9.2 r/w Clause 4.9.3 r/w Clause 4.9.4 of the DIP Guidelines). The promoters’ contribution will not be required in case of companies
where there is no identifiable promoter or promoter group.

**Minimum promoters’ contribution**

The promoters of the issuer shall contribute in the public issue as follows:

(a) in case of an initial public offer, not less than twenty per cent of the post issue capital.

(b) in case of a further public offer, either to the extent of twenty per cent of the proposed issue size or to the extent of twenty per cent of the post-issue capital.

(c) in case of a composite issue, either to the extent of twenty per cent of the proposed issue size or to the extent of twenty per cent of the post-issue capital excluding the rights issue component.

Lock-in of specified securities held by promoters

In a public issue, the specified securities held by promoters shall be locked-in for the period stipulated hereunder:

(a) minimum promoters’ contribution shall be locked-in for a period of three years from the date of commencement of commercial production or date of allotment in the public issue, whichever is later;

(b) promoters’ holding in excess of minimum promoters’ contribution shall be locked-in for a period of one year:

[Provided that excess promoters’ contribution as provided in proviso to clause (b) of regulation 34 shall not be subject to lock-in.]

**Explanation:** For the purposes of this clause, the expression "date of commencement of commercial production" means the last date of the month in which commercial production in a manufacturing company is expected to commence as stated in the offer document

These are some of the relevant topic which are often considered to be pre-requisite in equity issue in general and IPO issue in particular.
4.8 Pricing in public issue as prescribed by SEBI

1. An issuer may determine the price of specified securities in consultation with the lead merchant banker or through the book building process.

2. An issuer may determine the coupon rate and conversion price of convertible debt instruments in consultation with the lead merchant banker or through the book building process.

3. The issuer shall undertake the book building process in a manner specified in Schedule XI.

Differential pricing

An issuer may offer specified securities at different prices, subject to the following:

(a) Retail individual investors or retail individual shareholders may be offered specified securities at a price lower than the price at which net offer is made to other categories of applicants: Provided that such difference shall not be more than ten per cent of the price at which specified securities are offered to other categories of applicants.

(b) In case of a book built issue, the price of the specified securities offered to an anchor investor shall not be lower than the price offered to other applicants.

(c) In case of a composite issue, the price of the specified securities offered in the public issue may be different from the price offered in rights issue and justification for such price difference shall be given in the offer document.

Price and price band

(1) The issuer may mention a price or price band in the draft prospectus (in case of a fixed price issue) and floor price or price band in the red herring prospectus (in case of a book built issue) and determine the price at a later date before registering the prospectus with the ROC.

[Provided that the prospectus registered with the Registrar of Companies shall contain only one price or the specific coupon rate, as the case may be.]

(2) If the floor price or price band is not mentioned in the red herring prospectus,
the issuer shall announce the floor price or price band at least two working
days before the opening of the bid (in case of an initial public offer) and at
least one working day before the opening of the bid (in case of a further public
offer), in all the newspapers in which the pre issue advertisement was released.

(3) The announcement referred to in sub-regulation (2) shall contain relevant
financial ratios computed for both upper and lower end of the price band and
also a statement drawing attention of the investors to the section titled “basis
of issue price” in the prospectus.

(4) The cap on the price band shall be less than or equal to one hundred and
twenty per cent of the floor price.

(5) The floor price or the final price shall not be less than the face value of the
specified securities.

Explanation: For the purposes of sub-regulation (4), the “cap on the price band”
includes cap on the coupon rate in case of convertible debt instruments.

Face value of equity shares

Subject to the provisions of the Companies Act, 1956, an issuer making an initial
public offer may determine the face value of the equity shares in the following
manner:

(a) if the issue price per equity share is five hundred rupees or more, the issuer
shall have the option to determine the face value at less than ten rupees per
equity share: Provided that the face value shall not be less than one rupee per
equity share;

(b) if the issue price per equity share is less than five hundred rupees, the face
value of the equity shares shall be ten rupees per equity share:

[Provided that nothing contained in this sub-regulation shall apply to initial public
offer made by any government company, statutory authority or corporation or any
special purpose vehicle set up by any of them, which is engaged in infrastructure
sector.]
The disclosure about the face value of equity shares (including the statement about the issue price being “X” times of the face value) shall be made in the advertisements, offer documents and application forms in identical font size as that of issue price or price band.

4.8.1 Book building methodology: An Overview

Pricing of issue throughout the globe has drawn tremendous attention to all participants, both national and international, involved in new issue market. There are at least three distinct mechanisms adopted by the issuing firm: fixed price offer, book-building and auctions. Many countries in the world follow any one of these methods or combination of these pricing mechanisms. An issuer company is allowed to freely price the issue and disclose it in the offer document.

Book-building method of pricing IPOs came into operation as a consequence of the recommendations by the Malegam committee, set up by the SEBI in 1995. Initially, the method of book-building was not as popular as it is today but with the introduction and implementation of some major amendments and revisions it becomes very popular. It is basically a price and demand discovery mechanism by which the demand feedback of the investors applied for the IPO can be ascertained. It is an interactive process, a marked shift from the earlier process involving offer and acceptance under fixed price regime. SEBI guidelines defines Book Building as “a process undertaken by which a demand for the securities proposed to be issued by a body corporate is elicited and built-up and the price for such securities is assessed for the determination of the quantum of such securities to be issued by means of a notice, circular, advertisement, document or information memorandum or offer document”.

Book Building is basically a process used in Initial Public Offering for efficient price discovery. It is a mechanism where, during the period for which the IPO is open, bids are collected from investors at various prices, which are above or equal to the floor price. The offer price is usually determined after the bid closing date.

Here the investors themselves determine the price which they are willing to pay and what is acceptable to the issuer company. It helps to determine a realistically fair price as it is determined on the basis of bids made by the investors. The cost of
issue is generally reduced significantly and there are less chances of IPO under pricing. However, our results and earlier research reports in the same subject contradict this outcome.

Book building is a comparatively new concept for the Indian investors as compared to their peers in the U.S. or the U.K., where it is a very common practice. It is a process wherein various bids are collected from investors and the entries made in a book. It should be noted here that book building IPO is just another form of an IPO wherein investors, retail and institutional, can participate in the process and acquire shares of the company up for divestment or whose equity is at sale.

As per the SEBI Guideline, 2000 an issuer company can issue securities to the public through prospectus in the following manner:

1. 100% of the net offer to the public through book building process.
2. 75% of the net offer to the public through book building process and 25% at the price determined through book building. The fixed price portion is conducted like a normal public issue after the Book Built portion, during which the issue price is determined.

**Why Book Building?**

The abolition of the Capital Issue Contract Act, 1947 has brought a new era in the primary capital markets in India. Contracts over the pricing of the issues, designing and tenure of the capital issues were also abolished. The issuers, at present, are free to make the price of the issues. The main drawback of free pricing was the process of pricing of issues. The issue price was determined around 60-70 days before the opening of the issue and the issuer had no clear idea about the market perception of the price determined. The traditional fixed price method of tapping individual investors suffered from two major defects: (a) delays in the IPO process and (b) under-pricing of issue. Apart from these factors, the erstwhile free pricing era witnessed some anomalies by all the players operating in the IPO market. Some of them are listed as follows:-

- Inadequate disclosure in the prospectus by the promoters.
Misleading the investing public by decorating the prospectus with attractive projections which were often inflated.

Price rigged by the promoters by colluding with the brokers to justify higher prices to the investor. This was possible in the following ways:-

(i) Buying shares through intermediaries to camouflage the identity of promoters and thereby succeed in showing a healthy trend for their shares in the market.

(ii) This large scale buying triggers all around buying and price of these shares soar to a new height.

(iii) Later, these firms show inflated results as basis for the jump in their share prices.

(iv) Further, a right issue announcement justifies stepped up buying at higher prices.

Thus, it is required to find out a new mechanism for fair price discovery and to help the least informed investors. That’s why, book building mechanism, a new process of price discovery, has been introduced to overcome this aforesaid limitation and determine issue price effectively.

**Book Building Process in India**

A company wishing to adopt the route of Book Building is basically inviting the prospective buyers to subscribe their securities offered through prospectus. In fixed price process in IPOs, allotments of shares to all investors are made on proportionate basis. Institutional investors are not interested to participate in fixed price public issue due to uncertainty of attachment and lack of opportunity cost. On the other hand, they like to participate largely in book built transactions as in this process the cost of public issue and the time taken for the completion of the entire process are much less than fixed price method.

The main participant in the book building process are the issuer company, the Book Runner Lead Manager and the various syndicate members, who are the intermediaries are both eligible to act as underwriters.
Exhibit 4.3  
Participants in Book Building Process

Issuer

Book Runner

(Lead Manager)

SYNDICATE MEMBERS

Mutual Funds

Underwriters/
Merchant Bankers

Stock Brokers

SYNDICATE MEMBERS

Investors

Mutual Funds (MFs)

Financial Institutions (FIs)

Foreign Institutional Investors (FIIs)

Corporation

High Net-worth Individual (HNI)

Retail Investors

[Source: Agarwal, Sanjib: Bharat’s Manual of Indian Capital Market]

4.8.2 Regulatory Guidelines of Book building in India

The Book Building Guidelines were first introduced by SEBI in 1995 for optimum price discovery of corporate securities. The SEBI in its press release dated 7th September, 1998 prescribed the fresh Guidelines for book building mechanism after thorough modification and it was again modified in the year 2001 (Circular No.2, dated 06.12.2001) and 2003 (Circular No.11, dated 14.08.2003)
Exhibit 4.4

Steps involved in Book Building Process

Following are the major steps that are visible in any book building mechanism:-

1. Nominate Book Runner
2. Form Syndicate of Brokers, Arrangers, Underwriters, Financial institutions, etc.
3. Submit Draft offer Document to SEBI without mentioning Coupon Rate or Price
4. Circulate offer document among the Syndicate Members
5. Ask for Bids on Price and Quality of securities
6. Aggregate and forward all offer to Book Runner
7. Run the book to maintain a Record of subscribers and their orders
8. Consult with issuers and determine the issue price as weighted average of the offers received
9. Firm up underwriting commitments
10. Allot securities among syndicate members
11. Securities issued and listed
12. Trading commences on Exchanges

[Source: Agarwal, Sanjib: Guide to Indian Capital Market]
The following figure will clarify the theme of the book building process.

75% Book Building Method: Under this method of Book Building, 75% of the proposed issue or the 75% of the net offer to the public through book building route and the balance 25% of the issue is to be sold at a fixed price.

Exhibit 4.5

Source: Gangadhar and Reddy (2005), The Chartered Accountant November
As per the SEBI Guidelines, a public issue through Book Building route should consists of two portions: (a) the Book Building portion and (b) the fixed price portion.

Allotment to various investor categories is provided in the latest guidelines (2009) and is detailed below:

**In case of Book Built issue**

In case an issuer company makes an issue of 100% of the net offer to public through 100% book building process—

1. Not less than 35% of the net offer to the public shall be available for allocation to retail individual investors;

2. Not less than 15% of the net offer to the public shall be available for allocation to non-institutional investors i.e. investors other than retail individual investors and Qualified Institutional Buyers;

3. Not more than 50% of the net offer to the public shall be available for allocation to Qualified Institutional Buyers:

4. In case of compulsory Book-Built Issues at least 50% of net offer to public being allotted to the Qualified Institutional Buyers (QIBs), failing which the full subscription monies shall be refunded.

**In case of fixed price issue**

The proportionate allotment of securities to the different investor categories in a fixed price issue is as described below:

1. A minimum 50% of the net offer of securities to the public shall initially be made available for allotment to retail individual investors.

2. The balance net offer of securities to the public shall be made available for allotment to:

   (a) Individual applicants other than retail individual investors, and

   (b) Other investors including corporate bodies/ institutions irrespective of the number of securities applied for.
4.9 Recent development in IPO issue: A brief discussion

The following sections dealt with some of the pertinent issues which have gained popularity in the recent past in the IPO market under the aegis of SEBI are described below.

4.9.1 Green Shoe option

Green Shoe Option is a price stabilizing mechanism in which shares are issued in excess of the issue size, by a maximum of 15%. From an investor’s perspective, an issue with green shoe option provides more probability of getting shares and also that post listing price may show relatively more stability as compared to market volatility.

4.9.2 IPO Grading

A new initiative taken by the SEBI to appraise the retail investor’s about the fundamentals of the company going public through IPO process. IPO grading is the grade assigned by a Credit Rating Agency (CRAs) registered with SEBI to the initial public offering (IPO) of equity shares or any other security which may be converted into or exchanged with equity shares at a later date. The grade represents a relative assessment of the fundamentals of that issue in relation to the other listed equity securities in India. Such grading is generally assigned on a five-point scale with a higher score indicating stronger fundamentals and vice versa as below.

IPO grade 1 - Poor fundamentals
IPO grade 2 - Below-Average fundamentals
IPO grade 3 - Average fundamentals
IPO grade 4 - Above-average fundamentals
IPO grade 5 - Strong fundamentals

IPO grading has been introduced as an endeavour to make additional information available for the investors in order to facilitate their assessment of equity issues offered through an IPO.
4.9.3 **Eligibility criteria for listing at NSE**

An applicant who wishes to get listed its securities offered through IPO route with NSE must fulfill the following criteria:

1. **Paid-up capital**

   The paid up capital of the applicant shall not be less than ₹ 10 crore, for this purpose, the post-issue paid up capital for which listing is sought shall be taken into account and the capitalization of the equity shall not be less than ₹ 25 crore. For this purpose, the capitalization will be calculated as the product of the issue price and the post issue number of equity shares.

2. **Conditions precedent to listing**

   For listing in NSE the issuer need to adhere to the conditions precedent to listing as per the rules and regulations framed by the SEBI from time to time.

3. **At least three years track record of either**

   (a) The applicant seeking listing, or

   (b) The promoters/promoter company, incorporated in or outside India, here, promoter mean one or more persons with minimum three years of experience of each of them in the same line of business and shall be holding at least 20% of the post issue equity share capital either individually or severally. Or,

   (c) Partnership by firms and subsequently converted into a company (not in existence as a company for three years) and approach the exchange for listing. In this regard, the company seeking listing at the NSE must fulfill all the conditions stipulated by SEBI. For this purpose, the applicant or the promoting company shall submit annual reports of three preceeding financial years to NSE and also provide a certificate in respect to the following matters:

   I. The company has not been referred to the Board for Industrial and Financial Reconstruction (BIFR)

   II. The networth of the company has not been wiped out by the accumulated losses resulting in a negative networth
III. The company has not received any winding up petition admitted by a court. The applicant company desirous of listing its securities should also satisfy the exchange on the following points:

1. No disciplinary action has been initiated by other stock exchange and regulatory authorities in the past three years. There shall be no material regulatory or disciplinary action undertaken by a stock exchange or any other competent authority in the past 3 years against the applicant company in respect of promoters/promoting company or group companies.

2. Effectiveness of redressal mechanism of investor’s grievance. Track record of the applicant company’s redressal mechanism, the necessary infrastructure of the company in dealing with such issue and the general approach and philosophy to the issue of investor’s service and protection are considered here. Default made by the applicant company in respect to payment of interest and/or principal to the debenture/bond/fixed deposit holders by the applicant, promoter/promoting companies will also be evaluated. And in case of default in such payments, the securities of the applicant company may not be listed till such time it has been cleared and all pending obligations relating to the payment of interest and/or principal have been sorted out.

3. Distribution of shareholding pattern: the applicant company’s shareholding pattern on March 31st of preceeding three calendar years should be given specifying promoters and other groups’ shareholdings and whether it conforms to the regulatory requirement.

4. Details of litigation: the applicants/promoting company, group of companies litigation record, the nature of litigation, status of litigation during the preceding three years period need to be clarified to the exchange.

5. Track record of Directors of the Company: the track record of the directors, relevant disclosures may be insisted upon in the offer.
4.9.4 Role of SEBI in an Issue

Given below are the role played by SEBI in the context of primary and secondary capital markets:

(a) Till the early nineties, Controller of Capital Issues used to decide about entry of company in the market and also about the price at which securities should be offered to public. However, following the introduction of disclosure based regime under the aegis of SEBI, companies can now determine issue price of securities freely without any regulatory interference, with the flexibility to take advantage of market forces.

(b) The primary issuances are governed by SEBI in terms of SEBI (Disclosures and Investor Protection) Guidelines. SEBI framed its DIP guidelines in 1992 and over the years have gone through many amendments in keeping pace with the dynamic market scenario. It provides a comprehensive framework for issuing of securities by the companies.

(c) Before a company approaches the primary market to raise money by the fresh issuance of securities it has to make sure that it is in compliance with all the requirements of SEBI (DIP) Guidelines, 2000. The merchant banker are those specialised intermediaries registered with the SEBI, who perform the due diligence and ensures compliance with DIP Guidelines before the document is filed with SEBI. All issues are to be undertaken by category I Merchant Bankers authorized by the SEBI to do underwriting activities.

(d) Officials of SEBI at various levels examine the compliance with DIP guidelines and ensure that all necessary material information is disclosed in the draft offer documents.

(e) The requirement to issue shares at a par value of Rs.10 and Rs.100 was
withdrawn and that gave the companies the freedom to determine a fixed value per share.

(f) Any public issue where the price of each share is below Rs. 500, the face value of the shares should mandatorily be Rs. 10 per share. If the issue price is Rs. 500 or more, the minimum face value should not go below Rs. 1.

(g) The SEBI has also introduced the green-shoe option facility in IPOs as a stabilization tool for the post listing price stabilizing mechanism of newly issued shares.

(h) To enhance the level of investor protection, the process of dematerialization of securities through the depository system and their transfer through electronic book entry is made compulsory.

However, there are certain misconceptions prevailing in the mind of investors about the role of SEBI which are clarified here as under:

a) **SEBI does not recommend any Issue**

It should be distinctly understood that SEBI does not recommend any issue nor does it take any responsibility either for the financial soundness of any scheme or the project for which the issue is proposed to be made.

b) **SEBI does not approve the contents of an issue**

Submission of offer document to SEBI should not in any way be deemed or construed that the same has been cleared or approved by SEBI. The Lead manager certifies that the disclosures made in the offer document are generally adequate and are in conformity with SEBI guidelines for disclosures and investor protection in force for the time being. This requirement is to facilitate investors to take an informed decision for making investments in the proposed issue.

c) **SEBI observations on the offer document does not guarantee that the investment is safe**

The investors should make an informed decision purely by themselves based on the contents disclosed in the offer documents. SEBI does not associate itself with any issue/issuer and should in no way be construed as a guarantee
for the funds that the investor proposes to invest through the issue. However, the investors are generally advised to study all the material facts pertaining to the issue including the risk factors before considering any investment.

To conclude, this chapter deals with the rules and regulations as propounded by the various existing authorities from time to time to have a better understanding on the subject of issue management. Since our empirical work has been done with the NSE listed IPOs, we have considered it prudent to give a discussion on the eligibility requirement of NSE in case of IPOs. As it is already mentioned, the only objective of those stringent regulations is not only to aware the investors, both retail and institutional, but to alert the issuers companies about the fate of non-compliance and their consequence. Thus the chapters’ tries to fulfill the basics of the regulatory requirement under the auspices of SEBI in the light of the objectives we framed for our study.