CHAPTER IV

ROLE OF SEBI

INTRODUCTION

Why SEBI?

The ever expanding investor population and market capitalisation led to variety of malpractices on the part of companies, brokers, merchant bankers and others involved in new issues and stock in India.

The glaring examples of these malpractices are as under.

- Existence of self-styled merchant bankers, investment consultants without sufficient expertise and infrastructure for proper services.
- Unofficial private placements.
- Unofficial premium on new issues.
- Rigging up of prices.
- Manipulation of prices even before listing.
- Allotments with or without premium to the favoured persons.
- Delays in finalising the allotments and despatch of allotment letter, and refund order, before the due date.
- Violation of rules and regulations of the stock exchanges and listing requirements.
• Delay in delivery of shares and in making payments for sales by the brokers to their customers.

• Non-adherence of provisions of the Companies Act and other relevant Acts.

• Absence of fair practices in trading in the market such as rigging of shares, manipulation of prices, insider trading and a large spread between the bid and offer prices of jobbers.

• Problem of odd lots and poor liquidity of a number of shares in the secondary market.

• Diversion of funds of the mega issues for purposes other than that intended such as take over bids of other companies, acquisition of shares or investments of other companies and for working capital.

The malpractices and unfair trading practices have eroded investors' confidence. The Government and the Stock Exchanges were rather helpless in redressing the investor's problems because of lack of proper penal provisions in the existing legislature.

Realising this, SEBI was constituted by the Government in April 1988 as a supervisory body to regulate and promote the securities market.

An Act was passed to provide for the establishment of a Board to protect the interests of investors in securities and to promote the development of and to
regulate the securities market and for matters connected therewith or incidental thereto.

SEBI was constituted on 12th April, 1988 by a resolution passed by the government of India, Department of Economic Affairs as under.¹

"Whereas for sometime past the government of India had been concerned about the healthy growth of the securities market; and

"Whereas the government has satisfied that it was necessary to pass a comprehensive legislation for setting up a statutory apex Board to promote orderly and healthy growth of the securities market and for investor protection; and

Pending the enactment of such a legislation, it was necessary to constitute an interim body.

Therefore the government of India constituted the Securities and Exchange Board of India (SEBI) under the overall administrative control of the Ministry of Finance.

SEBI

• deals with all matters relating to development and regulation of securities market and investor protection, and advise government of these matters.

• Prepares a comprehensive legis.
  the securities market.
• Carries out such functions as may be
  the central government for the deve-
  lopment
• SEBI is free to determine its own proced-
  ed for records, returns, notes, memoranda, data
  to its working from official and non-offic
  ial discussions with them.
• SEBI has its head quarters in Bombay.
• SEBI submits reports to the government periodically on various aspects of
  the securities market and on such other specific matters as may be called for
  by the government.

LEGAL STATUS to SEBI

Initially, SEBI was established as an interim body under the
administrative control of the Finance Ministry until it was given statutory
powers recently. This has since been done and Statutory powers conferred on
SEBI vide the securities and Exchange Board of India ordinance, 1992. The
ordinance was later replaced by an Act of Parliament known as the
MANAGEMENT

- The management of SEBI vests with the board consists of a chairman, two member, amongst officials of the Ministries of the central Government dealing with Finance and Law; one member amongst officials of Reserve Bank of India and two other whole time members
- The general superintendence, direction and management of the affair, vests in the board of members.
- The terms and conditions may be laid down by the central government.
- The central government has the power to remove a member.
- The Board shall meet and observe such rules of procedures with regard to transaction of the business at its meetings.
- The Board appoints such officer, and employees as it deems fit.
- The vacancy etc., will not invalidate proceedings of the Board.

DUTIES of SEBI

SEBI has three duties cast upon it by the Act.²
- To protect the interests of investors in securities.
- To promote the development of the securities market.
- To regulate the securities market.

ORGANISATIONAL SET-UP

With a view to rationalising the operations and take up additional responsibilities, SEBI has recast its organisational set up. Its activities have been divided into five operational departments, each of which will be headed by senior official of the rank of Executive Director and reporting to the Chairman. The five departments are:

- Primary market policy, intermediaries and investor Grievance and Guidance department.
- The issue management and intermediaries Department.
- Secondary market, New investment products and Insider Trading Department.
- The Secondary Market Exchange Administration and Non-Member Intermediaries Department.
- Institutional investment, mergers and Acquisitions Research and Publications and International Regulations Department.

SEBI, with its head Quarters at Bombay, also intends to open regional offices in various parts of the country.

SALIENT FEATURES OF THE SEBI ACT

SEBI Act is deemed to have come into force on 30th January, 1992, the date of promulgation of the SEBI ordinance. The Bill to replace the ordinance was passed by both Houses of Parliament on 1st April, 1992 and became an
Act on 4th April, 1992, the date on which it received the assent of the President of India. The salient features of the SEBI are as under;

- The head office of the Board shall be at Bombay. The Board may establish offices at other places in India. In Bombay, the Board is situated at Mittal Court, B-wing, 224, Nariman point, Bombay - 400021.
- The Board will comprise of a chairman, two members representing the central governments, one member from RBI and two whole time members to be appointed by the central government.
- The SEBI shall be a body corporate by the name having perpetual succession and a common seal with power to acquire, hold and dispose of property, both movable and immovable, and to contract, and shall, by the said name, sue or be sued.
- The Board shall have necessary powers to protect the interest of investors in securities and will promote the development of and regulate the securities market.
- The general superintendence, direction and management of the affairs of the board are in a Board of Members, which may exercise all powers, and do all acts and things which may be exercised or done by that Board.
- The Government can prescribe terms of office and other conditions of service of the chairman and Member of the Board. The member, can be removed under section 6 of the SEBI Act under specified circumstances.
- In the exercise of its power, and performance of its functions, SEBI shall be bound by the policy directions of the central government.
FUNCTIONS OF SEBI

The following functions have been entrusted to the Board.

- Registering and regulating the working of stock brokers, sub-brokers, share transfer agents, bankers to an issue, trustees of trust deeds, registrars to an issue, merchant bankers, underwriters, portfolio managers, investment advisers and such other intermediaries who may be associated with securities markets in any manner.
- Registering and regulating the working of collective investment schemes including mutual funds.
- Regulating the business in stock exchanges and any other securities market.
- Promoting and regulating self-regulatory organisations.
- Prohibiting insider trading in securities.
- Promoting investor's education training of intermediaries of securities markets.
- Regulating substantial acquisition of shares and take over of companies.
- Calling for information from, undertaking inspection, conducting inquiries and audits of the stock exchanges and intermediaries and self-regulatory organisations in the securities market.
- Performing such functions and exercising such powers under the provisions of the SCR Act, as may be delegated to it by the central government.
- Levying fees or other charges for carrying out the purpose of the Act.

• Conducting research for the above purposes
• Prohibiting fraudulent and unfair trade practices relating to securities markets
• Performing such other functions as may be prescribed

ACHIEVEMENTS of SEBI

• Proper disclosure to investors through prospectus made obligatory.
• Guidelines for merchant bankers issued.
• Advertising code for mutual funds.
• Mutual funds required to publish balance sheets
• Take over code formulated.
• Draft guidelines on share transfer agents and registrars to an issue.
• Portfolio management service guidelines.
• Draft guidelines on insider trading.
• Stock invest scheme to eliminate delayed refunds.
• Suggested detailing brokerage/commission in contract notes.
• Set-up self-regulatory organisations like the Association of Merchant Bankers of India.
• Bombay Stock Exchange persuaded to pass a resolution admitting corporate members.
• Total ban on Forward Trading.
• Bombay Stock exchange has persuaded to publish outstanding trading position on some scrips.
• Registered a number of investor associations.
• Proposed that the exchanges take a percentage of the issue amount as deposit from companies seeking listing.
• Commenced registration of intermediaries associated with the stock exchange.
• Issued consultative paper on market pricing of securities.

CERTIFICATE OF REGISTRATION

Securities and Exchange Board of India, Merchant Bankers Rules were passed in the year 1992.

No stock-broker, sub-broker, share transfer agent, banker to an issue, trustee of trust deed, registrar to an issue, merchant banker, underwriter, portfolio manager, investment adviser and such other intermediary who may be associated with securities market shall buy, sell or deal in securities except under, and in accordance with the conditions of a certificate of registration obtained from the board in accordance with the rules made under this Act.

No person shall carry on any activity as a merchant banker unless he holds a certificate granted by the Board under the regulations;

Provided that such persons, who were engaged as merchant banker prior to the coming into force of the Act, may continue to carry on activity as merchant banker if he has made an application for such registration till the disposal of such application.
Conditions of Grant of Renewal of Certificate to Merchant Banker

The Board may grant or renew a certificate to a merchant banker subject to the following conditions, namely;

- The merchant banker, in case of any change in the status and constitution shall obtain the prior permission of the Board to carry on its activities as a merchant banker.
- He shall pay the amount of fees for registration or renewal, as the case may be, in the manner provided in the regulations.
- He shall take adequate steps for redressal of grievances of the investors within one month of the date of receipt of the complaint and keep the board informed about the number, nature and other particulars of the complaints received.
- He shall abide by the rules and regulations made under the Act in respect of the activities carried on by the merchant banker.

Period of validity of the certificate

The certificate of registration or its renewal, as the case may be, issued shall be valid for a period of three years from the date of its issue to the applicant.
REGISTRATION OF MERCHANT BANKER

Application for Grant of Certificate

According to Regulation 3(1), an application certificate shall be made to SEBI in Form I (Appendix II).

Regulation 3(2) provides for making the application for any one of the following categories of Merchant Banker:

Category I - to carry on any activity of the issue management, which will inter alia consist of preparation of prospectus and other information relating to the issue, determining financial structure, tie-up of financiers final allotment and refund of the subscription.

and

to act as advisor consultant, manager, underwriter and portfolio manager.

Category II - to act as Advisor, Consultant, Co-Manager, Underwriter, Portfolio manager.

Category III - to act as underwriter, Advisor, Consultant.

Category IV - to act only as Advisor or Consultant to an issue.

Thus as the gradation increases, the reaction decreases. The permissible activities of the categories are summarised in the following table:

Table 4.1

<table>
<thead>
<tr>
<th>Category</th>
<th>Manager</th>
<th>Advisor</th>
<th>Consultant</th>
<th>Cc Mana</th>
</tr>
</thead>
<tbody>
<tr>
<td>I</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>II</td>
<td>No</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>III</td>
<td>No</td>
<td>Yes</td>
<td>Yes</td>
<td>No</td>
</tr>
<tr>
<td>IV</td>
<td>No</td>
<td>Yes</td>
<td>Yes</td>
<td>No</td>
</tr>
</tbody>
</table>

Source: A practical guide to merchant banking.

Application to conform to the requirements

Regulation 4 provides for rejection of application by SEBI, if they are not complete in all respects and do not conform to instructions specified in the form. But before so rejecting, SEBI will give the applicant a reasonable opportunity to remove such deficits noted by SEBI. This rectification has to be effected by the applicant within the time allowed by SEBI.

Regulation 4 provides for rejection of incomplete applications or applications not conforming to the instructions specified in the form. However,
no application shall be rejected by SEBI till the applicant is given a reasonable opportunity of clearing the objections by SEBI within the time specified.

Furnishing of Information, Clarification and Personal Representation

• Regulation 5 empowers SEBI to direct an applicant to furnish further information or clarification regarding matters relevant to the activity of a Merchant Banker for the purpose of disposal of his application.
• It also empowers SEBI to require the applicant or its principal officer for personal representation.

Consideration of application

The Board shall take into account for considering the grant of a certificate, all matters which are relevant to the activities relating to merchant banker and in particular whether the applicant complies with the following requirements, namely:-

• the applicant has the necessary infrastructural facilities like adequate office space, equipments, and manpower to effectively discharge his activities.
• the applicant has in the employment minimum of two persons who have experience to conduct the business of Merchant Banking.
• person directly or indirectly connected with the applicant was not granted registration by SEBI (for the purpose of this clause, the expression"
"directly or indirectly connected" means Subsidiary inter-connected or Group Cor the applicant is a Body Corporate).

- the applicant fulfils the capital adeq regulation.

- the applicant, or his partner, or princip litigation connected with the securities m on the business of the applicant.

- the applicant, his director, partner or principal officer has not at any time been convicted for any offence involving moral turpitude or has been found guilty of any economic offence.

- the applicant has the professional qualification from an institution recognised by the Government in finance, law or business management.

- grant of certificate to the applicant is in the interest of investors.

Capital adequacy requirements

- The capital adequacy requirement of regulation 6 shall not be less than the net worth of the person making the application for grant of registration.

- For the purposes of sub-regulation (1), the net worth shall be as follows, namely:-

Regulation 7 specifies the capital adequacy norms for the categories I, II and III merchant bankers. No capital adequacy norms have been fixed for
category IV merchant bankers. For this purpose, the capital adequacy shall be computed as follows:-

- in case of a partnership firm/proprietorship business.

- in case of a company, the paid up capital

The net worth shall be computed as on the date of the application for a certificate.

Table 4.2
CAPITAL ADEQUACY OF MERCHANT BANKERS

<table>
<thead>
<tr>
<th>Category</th>
<th>Minimum Amount (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>I</td>
<td>50,00,000</td>
</tr>
<tr>
<td>II</td>
<td>50,00,000</td>
</tr>
<tr>
<td>III</td>
<td>20,00,000</td>
</tr>
<tr>
<td>IV</td>
<td>Nil</td>
</tr>
</tbody>
</table>

Source: A practical guide to merchant banking.

Regulation 8 provides for the manner of procedure to be followed by SEBI for grant of certificate, which are explained below.

- The Board on being satisfied shall grant a certificate mentioning the category.
- The applicant may apply to the Board after the expiry of one year from the registration date for higher category.
- The Board may consider an application made and grant a certificate.
- On the grant of a certificate the applicant shall be liable to pay the fees.
Provided that the amount of fees paid shall be reduced by the amount of fees already paid by the registered merchant bank in the category in which the registration is granted in the higher category.

On the grant of a certificate, the applicant shall pay fee applicable to the category in accordance with schedule.

Table 4.3
REGISTRATION FEES PAYABLE BY THE MERCHANT BANKERS

<table>
<thead>
<tr>
<th>Category</th>
<th>First two years</th>
<th>Third year</th>
</tr>
</thead>
<tbody>
<tr>
<td>I</td>
<td>Rs. 25 lakhs</td>
<td>Rs. 1 lakh</td>
</tr>
<tr>
<td>II</td>
<td>Rs. 1.5 lakhs</td>
<td>Rs. 50,000</td>
</tr>
<tr>
<td>III</td>
<td>Rs. 1 lakhs</td>
<td>Rs. 25,000</td>
</tr>
<tr>
<td>IV</td>
<td>Rs. 5000</td>
<td>Rs. 1000</td>
</tr>
</tbody>
</table>

Source: Guide to SEBI Capital Issues, Debentures and Listing

Table 4.4
RENEWAL FEES PAYABLE BY THE MERCHANT BANKERS

<table>
<thead>
<tr>
<th>Category</th>
<th>First two years</th>
<th>Third year</th>
</tr>
</thead>
<tbody>
<tr>
<td>I</td>
<td>Rs. 1 lakh</td>
<td>Rs. 20,000</td>
</tr>
<tr>
<td>II</td>
<td>Rs. 75,000</td>
<td>Rs. 10,000</td>
</tr>
<tr>
<td>III</td>
<td>Rs. 50,000</td>
<td>Rs. 5,000</td>
</tr>
<tr>
<td>IV</td>
<td>Rs. 5000</td>
<td>Rs. 2,500</td>
</tr>
</tbody>
</table>

Source: Guide to SEBI Capital Issues, Debentures and Listing

The fees shall be paid in the following manner:-

- First Instalment - with in 15 days from the date of intimation of registration by SEBI.
Subsequent instalments - on or before the expiry date of registration.

Where the applicant is granted registration in a later year, the annual fee payable shall be proportionately reduced by the amount on account of the year in which such registration is granted.

The fee structure prescribed have been considerably increased in the regulations. The SEBI circular had prescribed an authorisation fee of Rs.5 lakh, Rs 3 lakhs and Rs.1 lakh and annual fee of Rs 30,000, Rs 15,000 and Rs 5000 for categories I, II and III respectively.

Renewal of certificate

As it is stated above, a certificate of Authorisation granted by SEBI to a Merchant Banker is valid for a period of three years only from the date of grant by SEBI. After the expiry of the said period of three years, the applicant may submit a fresh application seeking renewal. These provisions are contained in Regulation.

Three months before the expiry of period of certificate, the merchant banker, if he so desires may make an application for renewal of the certificate granted to him. Such application shall also be in Form A.

The application for renewal shall be treated in the same manner as if it were a fresh application under the provisions of these Regulations.

SEBI on being satisfied that the applicant is eligible for renewal of Authorisation it may grant a certificate in Form B and send on intimation to
the applicant mentioning the category for which the Board has granted certificate

- If the renewal certificate is granted for lower category than that applied for, the applicant may make an application at any time after expiry of one year from the date of grant of such registration
- An application made for upgrading the category will be dealt with by SEBI in the same manner as it were a fresh application
- On granting the certificate, the applicant shall be liable to pay fees as per the Table of Fees given in schedule II to these regulations

**Procedure where Registration is not granted**

Regulation 10 deals with the procedure where registration is not granted, which are explained below

- If an application for grant of a certificate made under regulation 3 or an application for grant of renewal certificate made under regulation 9 does not satisfy the criteria provided in Regulation 6, SEBI may reject the application
- SEBI before rejecting so shall give an opportunity to the applicant of being heard
- Such refusal to grant registration shall be communicated by SEBI within thirty days of such refusal to the applicant stating the grounds on which the application has been rejected
The aggrieved applicant may within a period of thirty days from the date of receipt of such intimation to SEBI for reconsideration of its decision of rejection.

The Board shall reconsider an application made under sub-regulation (3) and communicate its decision as soon as possible in writing to the applicant.

**Effect of refusal to grant certificate**

Where an application does not satisfy the criteria set out in regulation 10, SEBI may reject the application after giving an opportunity of hearing to the applicant. Regulation 11 provides that, any Merchant Banker whose application for a certificate has been rejected by SEBI, shall on and from the date of the receipt of communication cease to carry on any activity as Merchant Banker. SEBI shall reconsider an application and communicate its decision in writing to the applicant.

**Payment of fees and the consequences of failure to pay fees**

According to Regulation 12, every applicant eligible for grant of certificate shall pay fees to SEBI in the manner within the period specified in schedule II.

Where a merchant banker fails to pay the Annual fees as provided in Sub-regulation (1), read with schedule II, the Board may suspend the registration certificate, where upon the merchant banker shall cease to carry on any activity as a merchant banker for the period during which the suspension subsists.
CODE OF CONDUCT

A merchant banker will be deemed to be guilty of misconduct or unprofessional conduct if he violates intentionally or otherwise any of the following provisions of the Code of Conduct. 7

- That the merchant banker herein agrees and undertakes to perform his duties as merchant banker with the highest standards of integrity and fairness in all his dealings

- The merchant banker and his personnel will act in an ethical manner in all his dealings with the investors, clients and fellow merchant bankers

- The merchant banker will inform the client before taking up any assignment that he is obliged to comply with the Code of Conduct of merchant bankers and he shall deliver a copy of the Code of Conduct to his client if he is not aware of or does not have it

- The merchant banker will render at all times high standards of service, exercise due diligence, ensure proper care and exercise independent professional judgement. The merchant banker will disclose to the clients his possible sources or potential areas of conflict of duties and interest while providing unbiased services

- No merchant banker will make any statement, indulge in any other acts or practices, indulge in any unfair competition, which may harm the interest of other members of the profession and put them in any disadvantaged position vis-à-vis him while competing for, or carrying out any assignment

7 The Securities and Exchange Board of India, Madras, Code of Conduct.
• The merchant banker will not make any statement either oral or written, which would misrepresent:

• The services that the merchant banker is capable of performing for the client, or has rendered to other clients subject to the secrecy he is expected to keep about clients' affairs

• The qualification of such merchant banker.

• The merchant banker will always endeavour to:

• give the best possible advice to the client in the context of client's needs and the environment, and his own professional ethics

• ensure that all professional dealings are rendered in a prompt, efficient and cost effective manner

• The merchant banker will not divulge the confidential information about a company which he has come across as a consequence of dealings with it to other clients, press or any other interested party. Further more he will not deal in the securities of the concerned client company, or when done, will make disclosures to the company's Board and SEBI

• Being fully aware of his obligation to investors, the merchant banker will endeavour to ensure that

• True and adequate information is provided to investors, no misleading or exaggerated claims or statements are made, and investor is made aware of attendant risks, before he takes an investment decision.
• Prompt and efficient services are rendered and got rendered in matters of
distribution of prospectus and related literature, allotment, refund and
queries of investors.
• A merchant banker will abide by all the provisions of the Acts, Rules,
Regulation, Guidelines, Resolutions, Notifications, Directions, Circulars
etc., issued by the Government of India and Securities and Exchange Board
of India from time to time as may be applicable to merchant bankers.

MAINTENANCE OF BOOKS OF ACCOUNTS, RECORDS, ETC.

• Regulation 14 provides for the maintenance of following Books of
Accounts, Records and Documents, namely:-
  • a copy of balance sheet as at end of the each accounting period;
  • a copy of profit and loss account for that period
  • a copy of the auditor's report on the accounts for that period; and
  • a statement of financial position.
• The merchant banker shall intimate SEBI, the place where the books of
accounts, records and documents are maintained
• Without prejudice to sub-regulation (1), every merchant banker shall, after
the end of each accounting period furnish to the Board copies of the
balance-sheet, profit and loss account and such other documents for any
other preceding five accounting years when required by the board.
SUBMISSION OF HALF YEARLY RESULTS

Every merchant banker shall furnish to SEBI half yearly unaudited financial results when required by it with a view to monitor capital adequacy norms of the merchant banker. (Regulation 15).

REPORT ON STEPS TAKEN ON AUDITORS REPORT

According to Regulation 17, every merchant banker shall within a period of two months from the date of Auditor's report, take steps to rectify the deficiencies made out in the Auditor's report.

APPOINTMENT OF LEAD MERCHANT BANKERS

Regulation 18 and 19 are the most significant ones, as they deal with appointment of merchant banker and restriction of maximum number of lead merchant bankers to an issue.

Regulation 18 provides that

- all issues shall be managed by at least one merchant banker functioning as the lead merchant banker.
- appointment of the minimum of one merchant banker is not required, in the case of rights issue, if the issue amount does not exceed a sum of the Rs. 50,00,000.
Every Lead merchant banker shall before taking up the assignment of an issue, enter into an agreement with the company setting out their mutual rights, liabilities, and obligations relating to such issue, and in particular to disclosures, allotment and refund.

Restriction on Appointment of Lead Managers

Regulation 19 regulates the appointment of maximum of head merchant bankers as follows:

Table 4.5
NUMBER OF LEAD MANAGERS
(Rupees in Crores)

<table>
<thead>
<tr>
<th>Size of Issue</th>
<th>Number of Lead Merchant Bankers. (Maximum)</th>
</tr>
</thead>
<tbody>
<tr>
<td>a</td>
<td>Less than 50</td>
</tr>
<tr>
<td>b</td>
<td>50 - 100</td>
</tr>
<tr>
<td>c</td>
<td>100 - 200</td>
</tr>
<tr>
<td>d</td>
<td>200 - 400</td>
</tr>
<tr>
<td>e</td>
<td>400 and above</td>
</tr>
</tbody>
</table>

Source: Master’s guide on SEBI

The number of Lead Merchant Bankers given above are maximum number that could be considered.

Responsibilities of Lead Managers

The specific responsibilities of lead managers are governed by Regulation 20.

• A merchant banker acting as a lead manager in connection with an issue, shall not associate so, unless his responsibilities relating to the issue are set out clearly, mainly with reference to the following matters.

- disclosures

- allotment and refund

A statement specifying such responsibilities are furnished to SEBI one month before the opening of an issue.

Where there are more than one Merchant banker to an issue, the responsibilities of each of them shall be furnished to SEBI atleast one month before the opening of an issue.

• A merchant banker can associate himself with an issue of its associate. Thus the restriction is only to act as lead merchant banker and a Merchant Banker could act in the capacity of a co-manager, Advisor or Consultant to an issue of its associate.

A Lead Merchant Banker is not to associate with a merchant banker without Registration:
According to Regulation 21, a lead merchant banker shall not be associated with an issue, if a merchant banker who is not holding certificate of registration is also associated with an issue.

**UNDERWRITING OBLIGATIONS**

In respect of every issue to be managed, the lead merchant banker holding a certificate under category I shall accept a minimum underwriting obligation of five percent of the total underwriting commitment or rupees twenty-five lakhs whichever is less.

Provided that, if the lead merchant banker is unable to accept the minimum underwriting obligation, that lead merchant banker shall make arrangement for having the issue underwritten to that extent by a merchant banker associated with the issue and shall keep the Board informed of such arrangement.

**SUBMISSION OF DUE DILIGENCE CERTIFICATE**

According to Regulation 23, the lead merchant banker, who is responsible for verification of the contents of a prospectus or the letter of office in respect of an issue and the reasonableness of the views expressed therein, shall submit to the Board at least two weeks prior to the opening of the issue for subscription, a due diligence certificate in Form C.
This is to ensure added authenticity for the correctness of facts and figures expressed in the offer documents.

DOCUMENTS TO BE FURNISHED TO THE BOARD

According to Regulation 24

- The Lead manager responsible for the issue shall furnish to SEBI, the following documents;
- particulars of the issue;
- draft prospectus or where there is an offer to the existing shareholders, the draft letter of offer;
- any other literature intended to be circulated to the investors; including the shareholders; and
- Such other relating to prospectus or letter of offer as the case may be.
- The documents referred to in sub-regulation (1) shall be furnished at least two weeks prior to date of filing of the draft prospectus or the letter of offer as the case may be with the Registrar of Companies or with the Regional Stock Exchanges or with both.
- The lead manager shall ensure that the modifications and suggestions, if any, made by the board on the draft prospectus or the letter of offer, as the case may be, with respect to information to be given to the investors are incorporated therein.
**Continuance of Association of Lead Manager with an issue**

Regulation 25, casts a specific responsibility on the merchant banker who is entrusted with the post-issue tasks.

It states that the lead manager undertaking the responsibility for refunds or allotment of securities in respect of any issue shall continue to be associated with the issue till the subscribers have received the share or debenture certificates or refund of excess application money.

The regulation further provides that, even if any other person other than the lead manager is entrusted with the refund or allotment of securities in respect of any issue, the lead manager shall continue to be responsible for the same.

**ACQUISITION OF SHARES PROHIBITED**

Regulation 26 is a piece of ethic to be followed by merchant banker, Director, partner or manager or principal officer of the merchant banker to enter into any transaction in securities of bodies corporate on the basis of unpublished price sensitive information obtained by them during the course of any professional assignment from the clients or otherwise. Violation of this regulation may end up in prosecution under SEBI (insider Trading) Regulation 1992.
This clause is relevant only for transaction having the following requisites:

- It should be entered to by the merchant banker or any of its directors, partners or principal officer
- It should be on the respective account of persons mentioned above or their associates or relatives
- It should be on the basis of unpublished price sensitive information
- Such information referred in (iii) above, should have been obtained by them during the course of any professional assignment either from the clients or otherwise

INFORMATION AND DISCLOSURES TO THE BOARD

As per Regulation 27, every merchant banker shall submit to the board complete particulars of any transaction for acquisition of securities of any body corporate whose issue is being managed by that merchant banker within fifteen days from the date of entering into such transaction.

Regulation 28 governs disclosures to be made by a merchant banker to SEBI. The following information should be disclosed as and when required by SEBI.

- his responsibilities with regard to the management of the issue;
- any change in the information or particulars previously furnished, which have a bearing as the certificate granted to it;
• the names of the body corporate whose issue he has managed or has been associated with;
• the particulars relating to breach of the capital adequacy requirements as specified in regulation 7;
• relating to his activities as a manager, underwriter, consultant and advisor to an issue, as the case may be.

RIGHT OF SEBI TO INSPECT

• Chapter IV of the Regulations (Regulation 29) empowers SEBI to inspect the books of accounts, records, and documents of the Merchant Banker for any of the purpose in the said regulations.
• The purposes referred to in sub-regulation (1) may be as follows namely:-
  • to ensure that the books of account are being maintained in the manner required.
  • that the provisions of the Act, rules and regulations are being complied with;
  • to investigate into the complaints received from investors, other merchant bankers or any other person on any matter having a bearing on the activities of the Merchant Banker.
  • to investigate suo moto in the interest of securities business or investors into the affairs of Merchant Bankers.

Notice before inspection

• According to Regulation 30, SEBI shall give a reasonable notice to the merchant banker before undertaking an inspection.
• Notwithstanding anything contained in sub-regulation (1) where the Board is satisfied that in the interest of the investors no such notice should be given, it may be an order in writing directing that the inspection of the affairs of the merchant banker to be taken up without such notice.

• During the course of inspection the merchant banker, against whom an inspection is being carried out, shall be bound to discharge his obligations as provided under regulation 31.

Obligations of the merchant bankers on inspection by SEBI

• Regulation 31 casts certain obligations on persons like every director, proprietor, partner, officer and employee of the merchant banker, who is being inspected, to produce such books, accounts and other documents and furnish him with statements and information within such time as the inspecting authority may require.

• The merchant banker who is being inspected shall allow the inspecting authority to have reasonable access to the premises occupied and also extend reasonable facility for examining any books, records, documents and computer data and also provide copies of documents or other materials which are relevant for the purpose of inspection.

• The inspecting authority in the course of inspection, shall be entitled to examine or record statement of any principal officer, Director, partner, proprietor, and employee of the merchant banker.
• It shall be the duty of every director, proprietor, partner, officer or employee of the merchant banker to give the inspecting authority all assistance in connection with inspection which the merchant banker may reasonably be expected to give.

Submission of Report to SEBI

The inspecting authority shall submit to SEBI the inspection report, as soon as may be possible, on his inspection of the merchant banker. (Regulation 32).

Communication of finding etc., to the Merchant Banker.

According to Regulation 33,

• The Board shall after consideration of the inspection report communicate the findings to the merchant banker to give him an opportunity of being heard before any action is taken by the board on the findings of the inspection authority.

• On receipt of the explanation, if any, from the merchant banker, the board may call upon the merchant banker to take such measures as the Board may deem fit in the interest of the securities market and for due compliance with the provisions of the Act, rules and regulations.
APPOINTMENT OF AUDITORS

Regulation 34 empowers SEBI to appoint a qualified auditor to investigate into the books of accounts or the affairs of Merchant Banker.

Provided that the auditor so appointed shall have the same powers of the inspecting authority as are mentioned in regulation 29 and the obligations of the merchant banker in regulation 31 shall be applicable to the investigation under this regulation.

PROCEDURE FOR ACTION IN CASE OF DEFAULT

Liability for action in case of default (Regulation 35)

- A merchant banker is liable to any of the penalties provided in the regulation, if he
  - Fails to comply with any conditions subject to which certificate has been granted.
  - contravenes any of the provisions of the Act, rules or regulations; shall be liable to any of the penalties specified in sub-regulation (2)
- The penalties referred to in sub-regulation (1) may be either:-
  - Suspension of registration; or
  - Cancellation of registration
Suspension of registration

• A penalty of suspension of registration of a merchant banker may be imposed where-
  • the merchant banker violates any of the provisions of SEBI Act, rules or regulations
  • the merchant banker-
  • fails to furnish any information relating to his activities as merchant banker as required by the board.
  • furnishes wrong or false information
  • does not submit periodical returns as required by the board;
  • does not co-operate in any enquiry conducted by the board.
  • the merchant banker fails to resolve the complaints of the investors or fails to give a satisfactory reply to the board in this behalf.
  • the merchant banker indulges in manipulating for price rigging or concerning activities.
  • the merchant banker is guilty of misconduct or unprofessional conduct which not in accordance with the code of conduct specified in schedule III.
  • the merchant banker fails to maintain the capital adequacy requirement in accordance with the provisions of regulation 7;
  • the merchant banker fails to pay the fees.
  • the merchant banker violates the conditions of registration.
  • the merchant banker does not carry out his obligations as specified in the regulation.
Cancellation of Registration

Regulation 37 provides for cancellation of registration in the following circumstances.

- If the merchant banker indulges in deliberate manipulation or price rigging or cornering activities affecting the securities market and the investors interest.
- If the financial position of the merchant banker deteriorates to such an extent that SEBI is of the opinion that his continuance as merchant banker is not in the interest of investors.
- If the merchant banker is guilty of fraud, or is convicted of a criminal offence.
- If the merchant banker makes repeated defaults of the nature mentioned in Regulation 36.

Manner of making order of suspension and cancellation

Regulation 38 provides that an order of suspension or cancellation of registration of a certificate granted to a merchant banker shall be imposed after holding an enquiry in accordance with the provisions of Regulation 39.

Manner of holding Enquiry before suspension or cancellation:
Regulation 39 governs matters relating to procedure of holding enquiry before an order of suspension or cancellation is made. These provisions are explained below:

- SEBI may appoint an enquiry officer for the purposes of holding enquiry under regulation 38.
- The enquiry officer shall issue to the merchant banker a notice at the registered office or the principal place of business of the merchant banker.
- The merchant bank may, within thirty days from the date of receipt of notices, furnish to the enquiry officer a reply together with copies of documentary or other evidence relied on by him or sought by the board from the merchant banker.
- The enquiry officer shall give the merchant banker a reasonable opportunity of being heard, to enable him to make submission's in support of his reply made under sub-regulation (3).
- The merchant banker may either appear before the enquiry officer in person or through any person duly authorised by the merchant banker;
- Provided that no lawyer or advocate shall be permitted to represent the merchant banker at the enquiry.
- Provided further that where a lawyer or an advocate has been appointed by the board as a presenting officer under sub-regulation (6), it shall be lawful for the merchant banker to present its case through a lawyer or advocate.
- The Enquiry officer, if required may request SEBI to appoint a presenting officer to present his case.
The Enquiry officer shall after taking into account all relevant facts and submissions made by the merchant banker, submit a report to SEBI and recommend penalty to be imposed as also the grounds on the basis of which the proposed penalty is justified.

Show-cause Notice and Order

Regulation 40 follows Regulation 39, with provisions for issuing show cause notice and order.

- On receipt of the report from the enquiry officer, the Board shall consider the same and issue a show-cause notice as to why the penalty as proposed by the enquiry officer should not be imposed.
- The merchant banker shall send his reply within twenty one days from the date of receipt of show cause.
- The board after considering the reply to the show-cause notice, if received, shall as soon as possible but not later than thirty days from the receipt of the reply, if any, pass such order as it deems fit.
- Every order passed under sub-regulation (3) shall be self-contained and give reasons for the conclusions stated therein including justification of the penalty imposed by that order.
- The Board shall send a copy of the order under sub-regulation (3) to the merchant banker.
Effect of suspension and cancellation of registration of merchant banker

According to Regulation 41

- On and from the date of the suspension of the merchant banker he shall cease to carry on any activity as a merchant banker during the period of suspension.
- On and from the date of cancellation the merchant banker shall with immediate effect cease to carry on any activity as a merchant banker.

Publication of order of suspension

The order made by SEBI either suspending or cancelling the certificate granted to a merchant banker shall be published at least in two daily newspapers by SEBI (Regulation 42).

Appeal to the central government

Regulation 43 enables an aggrieved merchant banker to prefer an appeal to the central government.

PERFORMANCE OF SEBI

After becoming a statutory body, SEBI has issued a number of guidelines and regulations and has undertaken a number of investigations for achieving its objectives, within a short span of one year.
A comprehensive guideline for disclosure and investor protection was issued by SEBI on June 11, 1992, which was followed by two clarification notes on such guidelines, issued on July 11 and July 16, 1992. The guidelines include pricing rules and disclosure rules with regard to first issue of companies.

SEBI has issued stringent regulations to curb the practice of insider trading. SEBI has also issued guidelines to regulate stock broker, and sub-brokers. Stock broker, in all recognised stock exchanges in the country are required to register themselves with SEBI. Every stock broker is required to keep and maintain the proper books of accounts, records etc., and intimate the place where the books are kept.

Another regulation towards investor protection is a regulatory framework for portfolio management services. SEBI has introduced compulsory registrations of portfolio managers.

The investors protection was SEBI's first priority and despite getting some flake in the MS Shoe issue controversy SEBI was taking appropriate action against those responsible for the fiasco.

Four companies had been given show causes and one of them was involved in the MS Shoe Issue, adding that thirteen merchant bankers had
already been issued show cause. Of these five were involved in the controversial issue.

SEBI has also asked MS Shoes to return the money of some 56,000 investors who have put their money in the issue which was only 39% subscribed.

To bring in more transparency, all these stock exchanges in the country had been asked to go in for computerisation, by SEBI.

Some of the companies delayed the share transfer. In this connection SEBI has already identified 20 such companies as major offenders in this connection and show cause notices have been already been in their names.

In case of open violation of SEBI guidelines that banks should keep an arms' length from their merchant banking subsidiaries came to light recently. SEBI has sought an explanation from the State Bank of India, on issuing an internal circular through which instructions were issued to fetch business for SBI Capital Markets, the merchant banking subsidiary of the SBI.

Apart from the existing controls which are now being exercised on merchant bankers, SEBI should also be given autonomy and wide ranging powers to discharge the duties and to give the investors a better deal.