CHAPTER - I

INTRODUCTION & REGULATORY FRAMEWORK FOR IPOs IN INDIA

The study is an attempt to monitor the pricing behavior of initial public offers in India. It is obvious to discuss the growth of the primary market and the regulatory framework for IPOs in India. Thus, these aspects have been covered in the first chapter of the study. The chapter has been categorized in three sections. The section one explains the introduction of primary market in India. Section two highlights the regulatory framework and various guidelines of Security Exchange Board of India regarding IPOs. Growth of the primary market has been analyzed in section three.

SECTION- I

INTRODUCTION OF PRIMARY MARKET

The capital market has a significant role to participate in economic development of a country. It is a prominent component of financial system. It aids economic growth by mobilizing the savings of the economic sectors and directing the same towards channels of productive use. Capital market can be categorized into two segments, Primary Market (New Issue Market) and Secondary Market (Stock market). Securities available for the first time are offered through new issue market. The issuer may be a new company or an existing company. In the new issue market the issuer can be considered as a manufacturer. Primary market facilitates long term flow of funds from surplus sector to the corporate sector.

The primary market deals with the new securities, but the outstanding securities are traded in the secondary market, which is commonly known as stock market. Secondary market is a mechanism, which provides liquidity, transferability and continuous price information
of securities to enable investors to buy and sell them with ease. The primary market deals with the ‘new’ securities i.e. which are not previously traded and are offered to the public for the first time. The securities issued in new issue market (NIM) are then traded in secondary market.

**Methods of New Issues:**

New issue in the primary market can be placed as Public offer, Offer for sale, Private placement and Right issue. It can be depicted as follows:-

Public Issue through Prospectus: This is the most popular method of raising capital from the general public. The company invites the public to subscribe the shares through the prospectus. The company gives the direct offer to the investing public to subscribe to the securities of the company at a given price. Prospectus contains the information like company’s name and address, names and addresses of directors, promoters, underwriters, bankers etc. Public issue can be categorized into two types, IPO & FPO.

Offer for sale: It is method of floatation of share through an "intermediary" and "indirectly" through an issue house for convert the private company into public company. In this case no need to issue prospectus. As per Section 70(i) of the Company Act, 1956 a statement in lieu of prospectus to be filled with Registrar of Companies at least 3 days before the allotment of securities.

Private Placement: The private placement means the direct sale of securities by a company to institutional investors or the issuing houses. They acquire the securities from the listing company at an agreed price and then they place the securities with their investor-clients.

Right Issue: According to Section 81 of the Company Act, 1956, if a company wants to increase its subscribed capital by allotment of further shares after two years from the date of its formation or one year from the
date of first allotment, it has to offer shares at first to the existing shareholders in proportion to the shares already held by them. It is called as right issue.

**Functions of New Issue Market:**

Primary Market or New Issue Market (NIM) performs three main functions i.e. Origination, underwriting and distribution of new securities.

Origination: The sponsors of issue do the work of investigation, analysis and review of the issue and render the consultative services, authenticating and processing services to the investors. All this work and service is called origination. This helps the issuing company in fixing the price, size of the issue, time of issue, terms and conditions of the issue and methods of flotation etc.

Underwriting: It is a promise made by a third party (underwriter) to the company issuing securities that underwriter will try to sale of securities and if part of securities remain unsold, the underwriter will itself subscribe to those securities.

Distribution: Sale of securities to ultimate investors is called distribution. It is a specialized job, which can be best performed by brokers and dealers in securities, who maintain direct and regular contact with ultimate investors.

**Terminology Regarding IPOs:**

Regarding IPOs few prominent terms must be discussed, these are:

Initial Public Offers (IPOs): An Initial public offers (IPOs) is a specific case of public issue, it is the first equity offering by a company to the public. It is the selling of securities to the public in the primary market. An IPO is defined as an exercise when an unlisted company makes either a fresh issue of securities or an offer for sale of its existing securities or both for the first time to the public. After allotment, the shares are listed on stock exchange to facilitate trading in them. In India
two methods of pricing are in practice: fixed price and book building. The shares are made available for the investors to invest at face value of the share or with a premium as per the perceived market value of the share by the promoter.

Red Herring Prospectus: It is a prospectus which does not have details of either price of number of shares being offered or the amount of issue.

Book Running Lead Manager (BRLM): It is a lead merchant banker appointed by the issuer company and whose name is maintained in the offer document of the issuer company.

Issue Price (Offer Price): It is the price at which equity share are offered to the public. IPOs are priced at par, premium.

Listing Day Price (List Price): It is the closing market price on the first day of trading in stock exchange. Generally, closing price of the listing day is taken to compute the underpricing.

Price Band: An issuer may mention a price/price band in the draft prospectus and floor price/price band in the red herring prospectus and determine the price at a later stage before registering the prospectus with ROCs. The cap on the price band/coupon rate should be up to a maximum 120 per cent of the floor price. The floor price should not be less than the face value.

Bids: In the Book-building method of IPO pricing company planning an IPO appoints a merchant Bank as a book runner collect bids from investors, which is based on a price band. The issue price is fixed after the closing date of the bids.

Floor price: Floor price is the minimum price at which bids can be made. The issuer company in consultation with the book-running lead manager fixes the floor price.

Issue size: Issue size refers to the total amount which is raised
through the public issue that is called issue size.

Opening Date of Issue: Opening Date is that date from which the bids will be accepted.

Closing date: The date on which offer will be closed is called closing date. The issue closes four to ten days after it opens.

Issue Price vs. listing day Price: Comparison of these two concepts is of great significance, as it helps in determining whether the shares are underpriced or overpriced.

Overpriced: If the offer price (Issue price) of share is more than the closing price of first trading day of listing, the share is said to be overpriced. It may be beneficial for the company in short run as it gets good amount of money. But it may not be advantageous in long run.

Underpriced: If the issue price of the shares is less than the closing price of the listing day, the share is said to be underpriced. It may help company to attract oversubscription of the issue. But it is an indirect cost of issue for company.

In fact both overpricing and underpricing are not good for the investors and the issuer in the long run. Therefore, the share should be issued at fair price.

**Pricing Practices of IPOs in India:**

Pricing method of IPOs adopted by CCI: The Capital Issues (Control) Act, 1947, enforced through the Office of Controller of Capital Issue (CCI) required the companies to obtain approval from CCI for raising capital. Prior to May 1992, new companies were allowed to issue shares only at par while existing companies with substantial reserves could issue shares at a premium that to be calculated by using pre determined equation given by CCI. These regulations are aimed at protecting the investors from overpricing.

Pricing method adopted by SEBI after abolition of CCI: The CCI
guidelines were abolished in May 1992 and Securities & Exchange Board of India (SEBI) has been formed under the SEBI Act, 1992. Under the new regime eligible companies have the freedom to issue shares at a price determined by themselves in consultation with the lead manager and giving justifications for the proposed premium by disclosing all the relevant information such that the investor can make an informed choice. During the period 1992 to 1999 the regulator played no role in the determination of the price and is solely left to the issuer but the investors have the choice to invest in it or leave it. In case of over subscriptions the allocation will be made on a pro-rata basis. The major disadvantage of this method is the price is determined solely by the issuers and the lead managers well in advance (atleast2-3 months prior to the offering) and is quite difficult for the lead manager to gauge the market clearing price. To compound the problem, if the issue is under-priced it will lead to oversubscription resulting in huge refunding costs. While in case of over-pricing, the issue may not be fully subscribed leading to devolvement and the lead manager's future business prospects will also be hampered.

The Y. H. Malegam Committee in 1995 recommended the introduction of book building as a mechanism to gauge the issue price from the market that is determined by demand and supply forces. However, it was in 1998 that SEBI brought forward the guidelines for issuing shares through the book building process. SEBI defines "book building as a process undertaken by which 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 securities to be issued by means of a notice, circular, advertisement, document or information memoranda or offer document"

New companies without a track record and companies who are not making profit are allowed to issue equity capital only at par value. The most common par value of share in India is 10 Rupees. Companies are
also required to state the price at which the public offering is to be made. The offer document (to be approved by SEBI) should provide an explanation as to why the offer price is considered reasonable.

**IPO Pricing Methods:**

There are basically two method of pricing IPOs viz.

1. Fixed Pricing
2. Book Building

Fixed Pricing: In the fixed price case, a price is decided upon for the issue by the merchant banker in consultation with the public company. This is the price at which investor can put in the application. This means the price is known upfront and hence investor can take the decision as to whether they want to put in the money or not. Traditionally, Indian IPOs used to be fixed price offerings, wherein prices of the stock on offer were determined prior to seeking investor’s bid. In fixed priced offerings, the offering of stocks is made without ascertaining the demand from investor and hence the price is discovered in the aftermarket.

Fixed Price Procedure:

Step 1: IPO price is decided by issuer after consultation with merchant banker
Step 2: Investors submit quantity bids
Step 3: Non discriminatory proportionate allocation

Book-Building: Book building essentially means that the “book is being built”. During the process on both NSE and BSE, investors can watch the book being built- a chart shown indicates the bid price and the number of shares being bid for. It helps to know the market price. It offers investors the opportunity to bid collectively. It then uses the bids to arrive at a consensus price. The process of book building is as:

- The company first of all appoints a Book Running Lead Manager
(BRLM).

- The BRLM prepares and submits the draft documents to the SEBI and obtains an acknowledgment card.
- The issuer and book runner decide the price within a specified price band.
- Offers at different price levels are invited from syndicate members, consisting of eligible brokers, merchant bankers, underwriters, financial institutions, mutual funds, and others. The advertisement should mention opening and closing dates for the bids.
- Based on the bids received, the issuer arrives at a final cut-off rate and the final allocation in consultation with the Book Running Lead Manager (BRLM).
- The issuer and the BRLM may impose restrictions on the number of shares that can be allotted to each client so as to avoid any future takeover threats.
- The final prospectus is filed with Registrar of Companies (ROC) along with the procurement agreement.
- The placement portion opens the subscription only after the prospectus is filed with ROC.
- The placement portion closes a day before the opening of the public issue portion.
- The public portion opens and the allotment and listing of this portion is done. The price determined in the book building process is applicable to the public portion as well. If the public portion stands oversubscribed, then the allotment is made on a proportionate basis. In case, the public portion remains undersubscribed, the shortfall is distributed amongst those who have opted for placement. If the placement portion is unsubscribed, the size of the public issue is enhanced.

**Difference between Book Building Issue and Fixed Price Issue:**
In Book Building securities are offered at prices above or equal to the floor prices, whereas securities are offered at a fixed price in case of a fixed price issue. In case of Book Building, the demand can be known everyday as the book is built. But in case of the fixed price issue the demand is known at the close of the issue.

**Eligibility Norms for launching IPO:**

The SEBI has laid down eligibility norms for entities raising funds through an IPO and an FPO. The entry norms are as follows:

**Entry Norm I:**

The Company desiring to tap the primary market shall meet the following requirements:

A. Net tangible assets of at least Rs. 3 crore for three full years, of which not more than 50 per cent is held in monetary assets.

B. Distributable profits in at least three out of the preceding five years.

C. Net worth of at least Rs. 1 crore in three years.

D. If there is a change in the company’s name, at least 50 per cent revenue for preceding one year should be earned from the new activity.

E. The issue size should not exceed 5 times the pre-issue net worth.

SEBI has provided two other alternative routes to a company not meeting any of the above mentioned requirements. They are as:

**Entry Norm-II:**

A. Issue shall be through a book building route, with at least 50 per cent of the issue to be mandatorily allotted to the qualified institutional buyers (QIB), failing which the money shall be refunded.

B. The minimum post-issue face value capital shall be Rs. 10 crore or
there shall be compulsory market making for at least 2 years.

OR

**Entry Norm-III:**

A. The project is appraised and participated to the extent of 15 per cent by FI/ schedule commercial banks of which at least 10 per cent comes from the appraiser(s).

B. The minimum post-issue face value capital shall be Rs. 10 crore or there shall be compulsory market making for at least 2 years.

In addition to satisfying the aforesaid eligibility norms, company shall be a compulsory having at least 1000 prospective allottees in its issue.

SEBI has exempted the following entities from entry norms:

- ✓ Private sector banks.
- ✓ Public sector banks.
- ✓ Right issue by listing company.
- ✓ An infrastructure company whose project has been appraised by PFI or IDFC or IL&FS or a bank which was earlier a PFI and not less than 5 per cent of the project cost is financed by any of these institutions.

According to Clause 2.2.2.B (v) of the DIP Guidelines, a QIB shall mean:

- A public financial institution as defined in sec. 4A of the companies Act, 1956;
- Scheduled commercial bank;
- Mutual fund;
- Foreign institutional investors registered with SEBI;
- Multilateral and bilateral development financial institutions;
- VCFs registered with SEBI;
• Foreign VCFs registered with SEBI;
• Provident funds with minimum corpus of Rs. 25 crore; and
• Pension funds with minimum corpus of Rs. 25 crore.

Process of Allotment:

The book building mechanism introduced in India in 1999 and has been active since then. Hence, presently both fixed price mechanism as well as book building mechanism exists in India. Over the years, companies have been shifting towards the book building mechanism. The reason is that book building is economically more efficient as more information is collected from investors following which price decision and allocation are made. In most other countries, the IPO allocation is discretionary i.e. allocation between retail and the institutional investors is in the hands of the underwriter. But in India it is not discretionary; underwriters have no discretion in making allocation between retail and the institutional investors. The allocation proportion in each category is known in advance. In fixed price IPOs, at least 50% of the shares must be made available to retail investors. In a book built issue allocation to Retail Individual Investors (RIIs), Non Institutional Investors (NIIs) and Qualified Institutional Buyers (QIBs) is in the ratio of 35: 15: 50 respectively. In case the book built issues are made pursuant to the requirement of mandatory allocation of 60% to QIBs in terms of rule 19(2)(b) of SCRR, the respective figures are 30% for RIIs and 10% for NIIs. This is a transitory provision pending harmonization of the QIB allocation in terms of the aforesaid Rule with that specified in the guidelines.

In India, the discretionary power given to the underwriter is only for the allocation to the Institutional investors. Institutional investors are also called Qualified Institutional Buyers (QIBs). Recently SEBI has also made a rule that from the QIBs segment, 5% should be allocated to the
Mutual funds. SEBI also allows a hybrid route. Book building could be used for a percentage, for example 75% of the issue could be with participation from institutions and large retail investors bidding more than the cutoff amounts for small investors, while the remaining 25% could be issued to small retail investors at the price determined in the book building process.

**Regulatory Constraints:**

In India, prior to 1992, regulatory requirements caused offer price to be set lower than perceived market prices. In India, new firms without a track record are not allowed to freely price the IPO. This regulatory factor is likely to result in greater under pricing.

It includes the growth of Indian primary market which provided the opportunity to millions of investors. In India, an IPO is also rated prior to listing on the basis of the disclosures made in their prospectus, not on the basis of quality or valuation of the issue. Although this rating does not tell anything about the issue and the firm but it serves as a signal to the retail investors in the market. The only limitation of Indian market is the data availability of short span of time i.e. two decades only while in other markets data is available for many decades.

Indian IPO market has grown rapidly with economic liberalization of 1990s. The regulatory body named the Controller of Capital Issues (CCI) was abolished and after some time in 1992, the Securities and Exchange Board of India (SEBI) was established as monitoring body of capital market in India, which gradually becomes powerful with the time. Prior to 1990s when CCI was existing, companies only with substantial reserves could issue shares on premium. This rule has changed by SEBI in 1992 and companies can issue shares on premium if generating a profit for last 3-5 years or if the promoting company having 50% post-IPO ownership has the same record. During CCI, the “CCI Formula” was used to calculate the fair price of equity on the basis of accounting information
which often led to extreme low prices due to consideration of book value; hence the debt was more preferred choice than equity (Shah, 1995). SEBI changed listing guidelines time to time during the decade to compete with world market resulting in transformation of Indian IPO market. The process of going public in India is almost similar to other developed countries, i.e. filing draft prospectus first with SEBI through with eligible investment banker and then filing to Registrar of Companies. The change in regulatory environment reformed the Indian primary market which resulted in huge rush toward going public. Some of the major implications are:

a. The offer price is chosen by firm and merchant banker, not using any fixed formula.

b. Approved offer price by SEBI can be increased by 20% to adjust listing delay effect.

c. Marketing of IPO is increased widely to appeal large number of investors.

d. The issue usually closes with 4-10 days and listing delay is also reducing gradually.

SECTION-II

REGULATORY FRAMEWORK FOR IPOs IN INDIA

The securities market is regulated by various agencies such as the Department of Economics Affairs, Department of Company Affairs, the Reserve Bank of India and the Securities and Exchange Board of India (SEBI). The role of SEBI is most important.

SEBI—Objectives and Functions

To protect the interest of investors and to develop and regulate the functioning of capital markets, the Securities and Exchange Board of India (SEBI) was setup through notification in April, 1988. The SEBI Act was passed on 4th April, 1992. It empowered SEBI to regulate activities
of primary and stock markets. SEBI exercises control over business in stock exchanges and other securities market, new issues registration, registering and regulation of market participants (like stockbrokers, sub-brokers, share transfer agents, bankers to an issue, registrars to an issue etc.), registering and regulating the working of venture capital fund, registering and regulating on collective investment schemes including mutual funds, regulating listing of securities, imposing a code of conduct merchant bankers/investment bankers, underwriters, brokers, etc., prohibition of fraudulent and unfair trade practices relating to securities markets and insider trading, promoting investors education, calling information for undertaking inspection, conducting inquiries and audits of stock markets, regulation substantial acquisition of shares and takeovers and conducting research for above purposes. SEBI also makes an attempt to establish and promote Self-regulatory organizations in securities market and ensures that stock exchanges discharge their self-regulatory role with efficiency and integrity.

As per SEBI Act, the objectives of the establishment of SEBI are to protect the interest of investors in securities market and to promote the development of and to regulate the securities market for matter concerned therewith or incidental therewith. The Preamble of the SEBI Act provides for the establishment of a Board. The following functions have been entrusted to the Board:

I. Regulating the business in stock exchanges and any other securities market.

II. Registering and regulating the working of stock brokers, sub-brokers, share transfer agents, bankers to an issue, merchant bankers, underwriters, portfolio managers, investment advisers and such other intermediaries who are associated with securities markets in any manner.

III. Registering and regulating the working of collective investment schemes.
schemes including mutual funds.

IV. Promoting and regulating self-regulatory organizations.

V. Prohibiting fraudulent and unfair trade practices relating to securities market.

VI. Promoting investors’ education and training of intermediaries of securities market.

VII. Prohibiting insider trading in securities.

VIII. Regulating substantial acquisition of shares and take-over of companies.

IX. Calling for information for undertaking inspection, conducting inquiries and audits of the stock exchanges, intermediaries and self-regulatory organizations in the securities market.

X. Calling for information and record from any bank or any authority or board or corporation established or constituted by or under any central, state or provincial Act in respect of any transaction in securities which is under investigated or inquiry by the Board.

XI. Performing such functions and exercising such powers under the provisions of Securities Contracts (Regulation) Act, 1956, as may be delegated to it by the Central Government.

XII. Levying fees or other charges for carrying out the above purposes.

XIII. Conducting research for the above purposes.

SEBI is expected to be responsive to the needs of the following participants of Indian financial system:

(a) The companies acquiring finance through equity and debt,

(b) Investors (shareholders and debenture holders),

(c) Primary market intermediaries (Bankers, Underwriters, Registrars, Lead Managers etc), and

(d) Stock –Exchange brokers, sub-brokers and other intermediaries.

Reforms of Primary Capital Market
The 1991-92 securities scam (Harshad Mehta) promoted the Indian
government to increase the speed of reforms in the capital market. The
following major reforms/developments have taken place recently related
to the primary market are following:

- The requirement of issue shares at a par value of Rs. 10 and Rs. 100
  was withdrawn.

- Foreign institutional investors were initially allowed to invest only
  in equity shares; later they were allowed to invest in the debt market,
  including dated government securities and treasury bills. The ceiling
  for investment by FIIs was increased from 40 percent to 49 percent
  in 2000-01. This increase can be made with the approval of
  shareholders through a special resolution in the general body
  meeting.

- Various bottlenecks on the floatation of new capital issues,
  particularly for infrastructure projects, were removed. Requirements
  such as making a minimum public offer on 25 per cent of the issue,
  five shareholders per Rs. 1 lac of offer, and a minimum subscription
  of 90 percentage no longer mandatory for infrastructure companies.

- With a view to promote the infrastructure companies raise funds for
  their project, their debt instruments are allowed to be listed on the
  stock exchange without prior listing of equity. The freedom to issue
  debt security without listing equity, till now granted to infrastructure
  companies and municipal corporations, has been extended to all
  companies. This is subject to certain conditions: Issues below Rs.
  100 crore shall carry an investment grade credit rating; issues above
  Rs. 100 crore shall carry an investment grade credit rating from two
  credit rating agencies; the issuer shall comply with the provisions of
  Rule 19 (2) (b) of the Securities Contracts (Regulation) Act (SCRA),
  1956 regarding the size of the public offer, and the promoters shall
  bring in the equity contribution of 20 per cent and lock in the same
  for three years.
• Merchant bankers are prohibited from carrying on fund based activities other than those related exclusively to the capital market. Multiple categories of MBs have been abolished and there is only one entity, the merchant banker.

• A code of conduct on advertisement has been issued for mutual fund, banning them from making any assurance or claims that might mislead the public.

• Besides merchant bankers various other intermediaries such as mutual fund, portfolio managers, registrars to an issue, share transfer agents, underwriters, debenture trustees, bankers to an issuer, custodian ,venture capital funds have also been brought under the purview of the SEBI.

• The entry norms for IPOs have been tightened by modifying the Disclosure and Investor Protection (DIP) Guidelines. According to the new guidelines, IPOs five times the size of the pre-issue net worth are allowed only if the company has had a record of profitability and a net worth of Rs. 1 crore in the three of the last 5 years. Companies without such a track record or an issue size beyond five times the pre-issue net worth are allowed to make IPOs through the book building route, with 60 per cent of the issue to be allotted to qualified institutional borrowers (QIBs).

• The SEBI DIP (Disclosure and Investor Protection) Guidelines, 2000 have been amended. The main provisions are as : permission to foreign venture capital registered with SEBI and State Industrial Development Corporations to participate in public issues through the book building route as Qualified Institutional Buyers (QIBs): no lock-in requirements for the pre-issue share capital of an unlisted company held by Venture Capital Funds (VCFs) and FVCIs; removal of exemption from public offer requirement in view of reduction in quantum from 25 per cent to 10 per cent; and removal of the
restriction of a minimum public issue size of Rs. 25 crore in respect of an IPO through the book building route.

**SEBI Guidelines for Issue of Securities**

The guidelines for issue of securities were first issued in 1992 and were amended subsequently from time to time. SEBI has now issued combined guidelines named SEBI (Disclosure and Investor Protection) Guidelines, 2000. These guidelines covered all public issues by listed and unlisted companies, all offers for sale and rights issues by listed companies whose equity share capital is listed, except in case of rights issues where the aggregate value of securities offered does not exceed Rs. 50 lac. The most relevant guidelines issued by SEBI are given as below:

1. **Eligibility Norms for Companies Issuing Securities**

(A) Filling of offer document (Clause 2.1):

(I) No issuer company shall make any public issue of securities, unless a draft Prospectus has been filed with the Board through a Merchant Banker, at least 30 days prior to the filing of the Prospectus with the Registrar of Companies (ROC) (Clause 2.1.1).

(II) No listed issuer company shall make any rights issue of securities, where the aggregate value of such securities, including premium, if any, exceeds Rs. 50 lac,) unless a draft letter of offer has been filed with the Board, through a Merchant Banker, at least 30 days prior to the filing of the letter of offer with the Designated Stock Exchange (DSE) (Clause 2.1.2).

(III) Fast Track Issues: Nothing contained in clauses 2.1.1 and 2.1.2 shall apply to a public issue of securities by a listed issuer company or a rights issue of securities by a listed issuer company, where the aggregate value of such securities, including premium, if any, exceeds Rs. 50 lac, if the following conditions are satisfied (Clause 2.1.2A.1):
(a) 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 reference date;

(b) The “average market capitalisation of public shareholding” of the company is at least Rs. 10,000 crore 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;

(c) 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;

(d) The company has redressed at least 95 per cent of the total shareholder / investor grievances or complaints received till the end of the quarter immediately preceding the month of the reference date;

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

(f) 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 per cent of the net profit/ loss after tax of the company for the respective years.

(g) 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

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

Explanation: For the purposes of this clause:

(*) “Reference date” shall mean:

(i) In case of a public issue of securities by a listed company satisfying all the requirements specified in this clause, the date of filing of red herring prospectus (in case of a book built issue) or prospectus (in case of a fixed price issue) with ROC; and

(ii) In case of a rights issue of securities by a listed company satisfying all the requirements specified in this clause, where the aggregate value of such securities, including premium, if any, exceeds Rs. 50 lac, the date of filing of letter of offer with Designated Stock Exchange.

(**) “Average market capitalisation of public shareholding” shall mean the sum of daily market capitalisation of “public shareholding” for a period of one year up to the end of the quarter preceding the month in which the proposed issue was approved by the Board/ shareholders, as the case may be, divided by the number of trading days. For this purpose, “public shareholding” shall have the same meaning as assigned to it in clause 40A of the Listing Agreement.

(IV) A listed issuer company satisfying all the requirements specified in this clause and filing a red herring prospectus (in case of a book built issue) or prospectus (in case of a fixed price issue) with ROC or letter of offer with Designated Stock Exchange, as the case maybe, shall simultaneously with such filing or as soon thereafter as reasonably practicable, but in any case not later than the opening of the issue, file a copy thereof with the Board (Clause 2.1.2A.2).
(V) No company shall make an issue of securities if the company has been prohibited from accessing the capital market under any order or direction of the Board (Clause 2.1.3).

(VI) No company shall make any public issue of securities unless it has made an application for listing of those securities in the stock exchange (Clause 2.1.4).

(VII) No company shall make public or rights issue or an offer for sale of securities (Clause 2.1.5), unless:

(a) The company enters into an agreement with a depository for dematerialisation of securities already issued or proposed to be issued to the public or existing shareholders; and

(b) The company gives an option to subscribers/ shareholders/ investors to receive the security certificates or hold securities in dematerialized form with a depository (Clause 2.1.5.1).

(B) Public issue by unlisted companies (Clause 2.2)

(I) An unlisted company shall make a Initial public issue of any equity shares or any security convertible into equity shares at a later date subject to the following(Clause 2.2.1):

a) The company has net tangible assets of at least Rs. 3 crore in each of the preceding 3 full years (of 12 months each), of which not more than 50% is held in monetary assets: Provided that if more than 50% of the net tangible assets are held in monetary assets, the company has made firm commitments to deploy such excess monetary assets in its business/project;

(b) The company has a track record of distributable profits in terms of Section 205 of the Companies Act, 1956, for at least three (3) out of immediately preceding five (5) years; Provided further that extraordinary items shall not be considered for calculating distributable profits in terms of Section 205 of Companies Act, 1956;
(c) The company has a net worth of at least Rs. 1 crore in each of the preceding 3 full years (of 12 months each);

(d) In case the company has changed its name within the last one year, at least 50% of the revenue for the preceding 1 full year is earned by the company from the activity suggested by the new name; and

(e) The aggregate of the proposed issue and all previous issues made in the same financial year in terms of size (i.e., offer through offer document + firm allotment + promoters’ contribution through the offer document), does not exceed five (5) times its pre-issue networth as per the audited balance sheet of the last financial year.)

(II) An unlisted company not complying with any of the conditions specified in Clause 2.2.1 may make an 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, only if it meets both the conditions (a) and (b) given below(Clause 2.2.2):

(a) (i) The issue is made through the book-building process, with at least 38(50% of net offer to public) being allotted to the Qualified Institutional Buyers (QIBs), failing which the full subscription money shall be refunded.

OR

(a) (ii) The “project” has at least 15% participation by Financial Institutions/Scheduled Commercial Banks, of which at least 10% comes from the appraiser(s). In addition to this, at least 10% of the issue size shall be allotted to QIBs, failing which the full subscription money shall be refunded

AND

(b) (i) The minimum post-issue face value capital of the company shall be Rs. 10 crore.
(b) (ii) There shall be a compulsory market-making for at least 2 years from the date of listing of the shares, subject to the following: (a) Market makers undertake to offer buy and sell quotes for a minimum depth of 300 shares; (b) Market makers undertake to ensure that the bid-ask spread (difference between quotations for sale and purchase) for their quotes shall not at any time exceed 10%; (c) The inventory of the market makers on each of such stock exchanges, as on the date of allotment of securities, shall be at least 5% of the proposed issue of the company.

(III) An unlisted public company shall not make an allotment pursuant to a public issue or offer for sale of equity shares or any security convertible into equity shares unless, in addition to satisfying the conditions mentioned in Clause 2.2.1 or 2.2.2 as the case may be, the prospective allottees are not less than one thousand (1000) in number. (Clause 2.2.2A):

For the purposes of clauses 2.2.1 and 2.2.2 above (Clause 2.2.2B):

(i) "Net Tangible Assets” shall mean the sum of all net assets of the company, 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 the monies proposed to be raised to cover the objects of the issue.

(iii) In case of partnership firms which have since been converted into companies, the track record of distributable profits of the firm shall be considered only if the financial statements of the partnership business for the said years 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 companies as per Schedule VI of the Companies Act, 1956;

b. The financial statements shall be duly certified by a Chartered Accountant stating that:

- The accounts as revised or otherwise and the disclosures made are in accordance with the provisions of Schedule VI of the Companies Act, 1956; and

- The accounting standards of the Institute of Chartered Accountants of India (ICAI) have been followed and that the financial statements present a true and fair picture of the firm’s accounts.

(iv) In case of an unlisted company 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.

(v) Offer for sale (Clause 2.2.3): An offer for sale shall not be made of equity shares of a company or any other security which may be converted into or exchanged with equity shares of the company at a later date, unless the conditions laid down in clause 2.2.1 or 2.2.2, as the case may be and in clause 2.2.2A, are satisfied(Clause 2.2.3.1), Offer for sale can also be made if provisions of clause 2.2.2 are compiled at the time of submission of offer document with Board(Clause 2.2.4).

(C) Public issue by listed companies (Clause 2.3)

(I) A listed company shall be eligible to make a public issue of equity shares or any other security which may be converted into or exchanged with equity shares at a later date(Clause 2.3.1): Provided that the aggregate of the proposed issue and all previous issues made in the same financial year in terms of size (i.e., offer through offer
document + firm allotment + promoters’ contribution through the offer document), issue size does not exceed 5 times its pre-issue networth as per the audited balance sheet of the last financial year.

Provided (further) that in case there is a change in the name of the issuer company within the last 1 year (reckoned from the date of filing of the offer document), the revenue accounted for by the activity suggested by the new name is not less than 50% of its total revenue in the preceding 1 full-year period.)

(II) Listed company which does not fulfill the conditions given in the provisions to Clause 2.3.1 above shall be eligible to make a public issue, subject to complying with the conditions specified in clause 2.2.2(Clause 2.3.2).

(III) Exemption from Eligibility Norms (Clause 2.4): The provisions of clauses (2.2 and 2.3) shall not be applicable in case of (Clause 2.4.1):

i) A banking company including a Local Area Bank (hereinafter referred to as Private Sector Banks) set up under sub-section (c) of Section 5 of the Banking Regulation Act, 1949 and which has received license from the Reserve Bank of India; or


iii) An infrastructure company:

a. Whose project has been appraised by a Public Financial Institution (PFI) or Infrastructure Development Finance Corporation (IDFC) or Infrastructure Leasing and Financing Services Ltd. (IL&FS) or a bank which was earlier a PFI; and)
b. Not less than 5% of the project cost is financed by any of the institutions referred to in sub clause (a), jointly or severally, irrespective of whether they appraise the project or not, by way of loan or subscription to equity or a combination of both;

iv) Rights issue by a listed company.

2. Pricing by Companies Issuing Securities

(A) The companies eligible to make public issue can freely price their equity shares or any security convertible at later date into equity shares in the following cases (Clause 3.0):

a. Public/ Rights Issue by Listed Companies (Clause 3.1)

A listed company whose equity shares are listed on a stock exchange, may freely price its equity shares and any security convertible into equity at a later date, offered through a public or rights issue (Clause 3.1.1)

b. Public Issue by Unlisted Companies (Clause 3.2)

An unlisted company eligible to make a public issue and desirous of getting its securities listed on a recognised stock exchange pursuant to a public issue, may freely price its equity shares or any securities convertible at a later date into equity shares(Clause 3.2.1).

(B) Infrastructure Company (Clause 3.2A)

An eligible infrastructure company shall be free to price its equity shares, subject to the compliance with the disclosure norms as specified by SEBI from time to time (Clause 3.2A.1).

(C) Initial Public Issue by Banks (Clause 3.3)

The banks (whether public sector or private sector) may freely price their issue of equity shares or any securities convertible at a later date into equity share, subject to approval by the Reserve Bank of India(Clause 3.3.1).
(D) Differential Pricing (Clause 3.4)

Any unlisted company or a listed company making a public issue of equity shares or securities convertible at a later date into equity shares, may issue such securities to applicants in the firm allotment category at a price different from the price at which the net offer to the public is made, provided that the price at which the security is being offered to the applicants in firm allotment category is higher than the price at which securities are offered to public (Clause 3.4.1).

(E) Price Band (Clause 3.5)

 Issuer company can mention a price band of 20% (cap in the price band should not be more than 20% of the floor price) in the offer documents filed with the Board and actual price can be determined at a later date before filing of the offer document with ROCs(Clause 3.5.1), If the Board of Directors has been authorised to determine the offer price within a specified price band such price shall be determined by a Resolution to be passed by the Board of Directors (Clause 3.5.2), The Lead Merchant Bankers shall ensure that in case of the listed companies, a 48 hours notice of the meeting of the Board of Directors for passing resolution for determination of price is given to the Designated Stock Exchange(Clause 3.5.3), In case of public issue by listed issuer company, issue price or price band may not be disclosed in the draft prospectus filed with the Board (Clause 3.5.4), In case of a rights issue, issue price or price band may not be disclosed in the draft letter of offer filed with the Board. The issue price may be determined anytime before fixation of the record date, in consultation with the Designated Stock Exchange (Clause 3.5.5) & The final offer document shall contain only one price and one set of financial projections, if applicable(Clause 3.5.6).

(F) Payment of Discounts/ Commissions (Clause 3.6)

No payment, direct or indirect in the nature of a discount, commission, and allowance or otherwise shall be made either by the
issuer company or the promoters in any public issue, to the persons who have received firm allotment in such public issue (Clause 3.6.1).

(G) Freedom to determine the denomination of shares for public / rights issues and to change the standard denomination (Clause 3.7)

An eligible company shall be free to make public or rights issue of equity shares in any denomination determined by it in accordance with Sub-section (4) of Section 13 of the Companies Act, 1956 and in compliance with the following and other norms as may be specified by SEBI from time to time (Clause 3.7.1):

i. In case of initial public offer by an unlisted company,
   a. If the issue price is Rs. 500/- or more, the issuer company shall have a discretion to fix the face value below Rs. 10/- per share subject to the condition that the face value shall in no case be less than Rs. 1 per share;
   b. If issue price is less than Rs. 500 per share, the face value shall be Rs. 10/- per share.

ii. The companies which have already issued shares in the denomination of Rs. 10/- or Rs. 100/- may change the standard denomination of the shares by splitting or consolidating the existing shares (Clause 3.7.2).

3. Promoters’ Contribution

(A) Promoters’ contribution in any issue shall be in accordance with the following provisions as on (Clause 4.0):

(i) The date of filing red herring prospectus (in case of a book built issue) or prospectus (in case of a fixed price issue) with ROC or letter of offer with Designated Stock Exchange, as the case may be, in case of a fast track issue; and

(ii) The date of filing draft offer document with the Board, in any other case.
(B) In a public issue by an unlisted company or offer for sale (Clause 4.1), the promoters shall contribute to not less than 20% of the post-issue capital (Clause 4.1.1).

(C) Promoters’ Shareholding in Case of Offers for Sale (Clause 4.2)

The promoters’ shareholding after offer for sale shall not be less than 20% of the post issue capital (Clause 4.2.1).

(D) Promoters’ Contribution in Case of Public Issues by Listed Companies (Clause 4.3)

In case of public issues by listed companies, the promoters shall participate either to the extent of 20% of the proposed issue or ensure post-issue share holding to the extent of 20% of the post-issue capital (Clause 4.3.1).

(E) In case of public issues or composite issues by listed companies (Clause 4.4), the promoters shall participate to the extent of 20% of post-issue capital (Clause 4.4.1).

(F) Securities Ineligible for Computation of Promoters’ Contribution (Clause 4.6) If promoters have acquired equity during proceeding three years for consideration other than cash or by way of bonus shares, such shares shall not be considered for computation of promoters’ contribution (Clause 4.6.1).

(G) In case of public issue by unlisted companies, securities which have been issued to the promoters during the proceeding one year, at a price lower than the price at which equity is being offered to public shall not be eligible for computation of promoters’ contribution. However, if promoters bring the difference, after passing necessary resolutions and filing of revised returns of allotment, the shares shall be considered eligible (Clause 4.6.2).

(H) Promoters’ Participation in Excess of the Required Minimum Contribution to be Treated as Preferential Allotment (Clause 4.8) In
case of a listed company, participation by promoters in the proposed public issue in excess of the required minimum percentage referred in Clauses 4.3.1 and 4.4.1 shall attract the pricing provisions of Guidelines on preferential allotment, if the issue price is lower than the price as determined on the basis of said preferential allotment guidelines (Clause 4.8.1).

(I) Promoters’ Contribution to be brought in before Public Issue Opens

(Clause 4.9) Promoters shall bring in the full amount of promoters contribution including premium at least one day prior to the issue opening date which shall be kept in an escrow account with a scheduled commercial bank and the said among shall be released to the company along with the public issue proceeds (Clause 4.9.1):

Provided that, where the promoter’s contribution has been brought prior to the public issue and has already been deployed by the company, the company shall give the cash flow statement in the offer document disclosing the use of such funds.

Provided, further, that where the promoters minimum contribution exceeds Rs. 100 crore, the promoters shall bring in Rs. 100 crore before the opening of the issue and the remaining contribution shall be brought in by promoters in advance on pro-rata basis before the calls are made on public.

(J) Exemption from Requirement of Promoters’ Contribution (Clause 4.10) The requirement of promoters contribution shall not be applicable if (a) the company is listed on a stock exchange for at least 3 years and has a track record of dividend payment for at least three immediately preceding years; (b) in case of companies where no identifiable promoter or promoter group exists, and (c) in case of rights issues. However, in case of (a) and (c), the promoters shall disclose existing shareholding in the offer document (Clause 4.10.1).
4. Lock-in of Minimum Specified Promoters Contribution (Clause 4.11)

(A) In case of any issue of capital to the public the minimum promoters’ contribution (as per clause 4.1, 4.2, and 4.3 (and) shall be locked in for a period of 3 years (Clause 4.11.1) The lock-in shall start from the date of allotment in the proposed public issue and the last date of the lock in shall be reckoned as three years from the date of commencement of commercial production or the date of allotment in the public issue whichever is earlier. Thus, the normal lock in period is 3 years (Clause 4.11.2).

(B) In case of a public issue by unlisted company, if the promoters’ contribution in the proposed issue exceeds the required minimum contribution, such excess contribution shall also be locked-in for a period of 1 year (Clause 4.12.1).

(C) In case of a public issue by a listed company, the excess shall be locked in for a period of 1 year as per the lock-in provisions prescribed in guidelines on preferential issues (Clause 4.12.2).

(D) If shortfall in the firm allotment category is met by the promoters, it will be locked-in for a period of one year (Clause 4.12.3).

(E) The entire pre-issue share capital, other than that locked-in as promoter’s contribution shall be locked-in for a period of one year from the date of commencement of commercial production or the date of allotment in the public issue, whichever is later (Clause 4.14.1).

(F) Locked-in securities held by promoters may be pledged only with banks or financial institutions as collateral security for loans (Clause 4.15.1).

(G) Transfer of locked-in securities amongst promoters as named in the offer document, can be made subject to the lock-in being applicable
to the transferees for the remaining period of lock-in (Clause 4.16.1).

(H) The securities which are subject to lock-in shall carry inscription ‘non-transferable’ along with duration on the face of the security certificates (Clause 4.17.1).

5. **Pre-issue Obligations**

The SEBI (DIP guidelines, 2000) also explain about the pre issue obligation. The issuer company has to fulfill these following obligations:

(A) Documents to be submitted (Clause 5.3): The lead manager shall submit

following document to SEBI:

(i) Memorandum of Understanding (MOU) between lead merchant banker and issuer company.

(ii) Inter-se Allocation of Responsibilities.

(iii) Due diligence certificate by lead merchant banker as specified in Schedule III, along with draft prospectus.

(iv) Certificates signed by the company secretary or chartered accountant in case of listed companies making further issue of capital.

(v) Undertaking- The issuer shall submit an undertaking to the Board to the effect that transactions in securities by the 'promoter' the 'promoter group' and the immediate relatives of the 'promoters during the period between the date of filing the offer documents with the Registrar of Companies or Stock Exchange as the case may be and the date of closure of the issue shall be reported to the Stock exchanges concerned within 24 hours of the transaction(s).

(vi) List of the promoters group and their details.
(B) Appointment of intermediaries (clause 5.4.3)

(C) Underwriting (clause 5.5): The lead merchant banker shall satisfy themselves about the ability of the underwriters to discharge their underwriting obligations. In respect of every underwritten issue, the lead merchant bankers shall undertake a minimum underwriting obligation of 5% of the total underwriting commitment or Rs. 25 lac whichever is less. The outstanding underwriting commitments of a merchant banker should not exceed 20 times its networth at any point of time.

(D) Offer documents to be made public( clause 5.6) : The draft offer document filed will the Board shall be made public for a period of 21 days from the date of filing the offer document with the Board.

(E) IPO Grading (clause 5.6B): Every unlisted company obtaining grading for IPO under clause 2.5A.1 shall disclose all the grades obtained, along with the rationale/ description furnished by the credit rating agency(ies) for each of the grades obtained, in the Prospectus, Abridged Prospectus, issue advertisements and at all other places where the issuer company is advertising for the IPO.

(F) Dispatch of issue material( clause 5.7): The lead merchant banker shall ensure that for public issues offer documents and other issue materials are dispatched to the various stock exchanges, brokers, underwriters, bankers to the issue, investors associations, (Self Certified Syndicate Banks) etc. in advance as agreed upon.

(G) Authorized collection centres (clause 5.10): The issuer company can also appoint authorized collection agents in consultation with the Lead Merchant Banker subject to necessary disclosures including the names and addresses of such agents made in the offer document.

6. Guidelines on Advertisement

According to SEBI (DIP guidelines), “Advertisement” includes notices, brochures, pamphlets, circulars, show cards, catalogues,
hoardings, placards, posters, insertions in newspaper, pictures, films, cover pages of offer documents or any other print medium, radio, television programmes through any electronic medium;

The following are some of the main guidelines on advertisement:

(A) An issue advertisement shall be truthful, fair and clear and shall not contain any statement which is untrue or misleading (Clause 9.1.0).

(B) Any advertisement reproducing or purporting to reproduce any information contained in a offer document shall reproduce such information in full and disclose all relevant facts and not be restricted to select extracts relating to that item(Clauses 9.1.1).

(C) An issue advertisement shall be considered to be misleading, if it contains (Clause 9.1.2):

(a) Statements made about the performance or activities of the company in the absence of necessary explanatory or qualifying statements, which may give an exaggerated picture of the performance or activities, than what it really is.

(b) An inaccurate portrayal of past performance or its portrayal in a manner which implies that past gains or income will be repeated in the future.

(D) An advertisement shall be set forth in a clear, concise and understandable language (Clause 9.1.3).

(E) An issue advertisement shall not contain statements which promise or guarantee rapid increase in profits (Clause 9.1.4).

(F) An issue advertisement shall not contain any information that is not contained in the offer document (Clause 9.1.5).

(G) No models, celebrities, fictional characters, landmarks or caricatures or the likes shall be displayed on or form part of the offer documents or issue advertisements (Clause 9.1.6).
(H) Issue advertisements shall not appear in the form of crawlers (the advertisements which run simultaneously with the programme in a narrow strip at the bottom of the television screen) on television (Clause 9.1.8). In case of issue advertisement on television screen:

(a) the risk factors shall not be scrolled on the screen; and

(b) the advertisement shall advise the viewers to refer to the red herring prospectus or other offer document for details.

(I) No advertisement shall include any issue slogans or brand names for the issue except the normal commercial name of the company or commercial brand names of its products already in use (Clause 9.1.9).

(J) No slogans, expletives or non-factual and unsubstantiated titles shall appear in the issue advertisements or offer documents (Clause 9.1.10.)

(K) If any advertisement carries any financial data, it shall also contain data for the past three years and shall include particulars relating to sales, gross profit, net profit, share capital, reserves, earnings per share, dividends and the book values (Clause 9.1.11).

(L) It shall contain the names of Issuer Company, address of its registered office, names of the main lead merchant bankers and registrars to the issue (Clause 9.1.12).

(M) No issue advertisement shall be released without giving “Risk Factors” in respect of the concerned issue, provided that an issue opening/closing advertisement which does not contain the highlights need not contain risk factors (Clause 9.1.13).

(N) All public communications and publicity material, including corporate and product advertisements of the issuer company, interviews by its promoters, directors, duly authorized employees
or representatives of the issuer company, documentaries about the
issuer company or its promoters, periodical reports and press
releases, issued or published in any media during the period
commencing from the date of filing draft offer document with
SEBI till the date of allotment of securities offered in the issue,
shall comply with the following(Clause 9.1.14A):

(a) It shall be prominently displayed or announced in such public
communication or publicity material that the issuer company is
proposing to make a public or rights issue of securities, as the
case may be and has filed a draft offer document with SEBI or
has filed the Red Herring Prospectus / Prospectus with the
Registrar of Companies or the Letter of Offer with the
Designated Stock Exchange, as the case may be.

(b) It shall further be stated in such public communication or
publicity material that the draft offer document, Red Herring
Prospectus or final offer document, as the case may be, is
available on SEBI website at www.sebi.gov.in as well as on
the Lead Managers’ websites <urls to be given>.

(c) Such public communication or publicity material shall contain
only factual information and shall not contain projections,
estimates, conjectures etc.

(d) Such public communication or publicity material shall also not
contain any information which is extraneous to the draft offer
document filed with SEBI or the Red Herring Prospectus /
Prospectus filed with the Registrar of Companies or the Letter
of Offer filed with Designated Stock Exchange, as the case
may be. The issuer company shall make prompt, true and fair
disclosure of all material developments taking place during the
period mentioned hereunder, relating to its business and
securities and also relating to the business and securities of its
subsidiaries, group companies, etc., which may have a material effect on the issuer company, by issuing public notices in all the newspapers in which the issuer company had issued pre-issue advertisement under clause 5.6.A:

- In case of a fixed price public issues, between the date of filing final prospectus with the Registrar of Companies and the date of allotment of securities offered in the public issue.

- In case of a book built issue, between the date of filing the Red Herring Prospectus with the Registrar of Companies and the date of allotment of the securities offered in the issue.

- In case of a rights issue, between the date of filing the Letter of Offer with the Designated Stock Exchange and the date of allotment of the securities offered in the rights issue (Clause 9.1.14B).

(O) No corporate advertisement of Issuer Company shall be issued after 21 days of the filing of the offer document with the Board till the closure of the issue unless the risk factors as are required to be mentioned in the offer document, are mentioned in such advertisement (Clause 9.1.15).

(P) No product advertisement of such company shall contain any reference directly or indirectly to the performance of the company during the specified period (Clause 9.1.16).

7. **Guidelines on IPOs through the On-Line System (E-IPO)**

A company proposing to issue capital to public through the on-line system of the stock exchange for offer of securities shall comply with the requirements as contained in this Chapter in addition to other requirements for public issues as given in these Guidelines, wherever applicable (Clause 11A.1).
(A) Agreement with the Stock exchange (Clause 11A.2)

   The company shall enter into an agreement with the Stock Exchange(s) which have the requisite system of on-line offer of securities (Clause 11A.2.1).

(B) Appointment of Brokers (Clause 11A.3)

   The stock exchange, shall appoint brokers of the exchange, who are registered with SEBI, for the purpose of accepting applications and placing orders with the company (Clause 11A.3.1). For the purposes of this Chapter, the brokers, so appointed accepting applications and application monies, shall be considered as ‘collection centre’s (Clause 11A.3.2). The broker/s so appointed, shall collect the money from his/their client for every order placed by him/them and in case the client fails to pay for shares allocated as per the Guidelines, the broker shall pay such amount (Clause 11A.3.3). The company/lead manager shall ensure that the brokers having terminals are appointed in compliance with the requirement of mandatory collection centre’s, as specified in clause 5.9 of Chapter V (Clause 11A.3.4). The company/lead manager shall ensure that the brokers so appointed are financially capable of honouring their commitments arising out of defaults of their clients, if any (Clause 11A.3.5). The company shall pay to the broker/s a commission/fee for the services rendered by him/them. The exchange shall ensure that the broker does not levy a service fee on his clients in lieu of his services (Clause 11A.3.6).

(C) Appointment of Registrar to the Issue (Clause 11A.4)

   The company shall appoint a Registrar to the Issue having electronic connectivity with the Stock Exchange/s through which the securities are offered under the system (Clause 11A.4.1).

(D) Listing (Clause 11A.5)

   The company may apply for listing of its securities on an exchange
other than the exchange through which it offers its securities to public through the on-line system (Clause 11A.5.1).

(E) Responsibility of the Lead Manager (Clause 11A.6)

The Lead Manager shall be responsible for co-ordination of all the activities amongst various intermediaries connected in the issue/system. The names of brokers appointed by the issuer company along with the names of the other intermediaries namely lead managers to the issue and Registrars to the Issue shall be disclosed in the prospectus and application form (Clause 11A.6.1).

(F) Mode of Operation (Clause 11A.7)

(i) The company shall, after filing the offer document with ROC and before opening of the issue, make an issue advertisement in One English and One Hindi daily with nationwide circulation and one regional daily with wide circulation at the place where the registered office of the issuer company is situated (Clause 11A.7.1).

(ii) The advertisement shall contain the salient features of the offer document as specified in Form 2A of the Companies (Central Government’s) General Rules and Forms, 1956. The advertisement in addition to other required information shall also contain the following (Clause 11A.7.2):

(a) The date of opening and closing of the issue;
(b) The method and process of application and allotment;
(c) The names, address and the telephone numbers of the stock brokers and centres for accepting the applications (Clause 11A.7.3).

(iii) In case of issue of capital of Rs. 10 crore or above the Registrar to the Issue shall open centres for collection of direct applications at the four metropolitan centres situated at Delhi, Chennai, Kolkata and Mumbai (Clause 11A.7.4).
(iv) The broker shall collect the client registration from duly filled up and signed from the applicants before placing the order in the system as per “Know your client role” as specified by SEBI and as may be modified from time to time(Clauses 11A.7.5).

(v) The broker shall, thereafter, enter the buy order in the system, on behalf of the clients and enter details including the name, address, telephone number and category of the applicant, the number of shares applied for, beneficiary ID, DP code, etc. and gives an order number/order confirmation slip to the applicant (Clause 11A.7.6).

(vi) The applicant may withdraw applications in terms of the Companies Act, 1956(Clauses 11A.7.7).

(vii) The broker may collect an amount to the extent of 100% of the application money as margin money from the clients before he places an order on their behalf (Clause 11A.7.8).

(viii) The broker shall open a separate bank account [Escrow Account] with the clearing house bank for primary market issues and the amount collected by the broker from his clients as margin money shall be deposited in this account(Clauses 11A.7.9).

(ix) The broker shall, at the end of each day while the issue is open for subscription, download/forward the order data to the Registrar to the Issue on a daily basis. This data shall consist of only valid orders (excluding those that are cancelled). On the date of closure of the issue, the final status of orders received shall be sent to the Registrar to the issue/company (Clause 11A.7.10).

(x) On the closure of the issue, the Designated Stock Exchange, along with the Lead merchant banker and Registrars to the Issue shall ensure that the basis of allocation is finalised in fair and proper manner on the lines of the norms with respect to basis of allotment
as specified in Chapter VII of the Guidelines, as may be modified from time to time (Clause 11A.7.11).

(xi) After finalisation of basis of allocation, the Registrar to the Issue/company shall send the computer file containing the allocation details i.e. the allocation numbers, allocated quantity, etc., of successful applicants to the Exchange. The Exchange shall process and generate the broker-wise funds pay-in obligation and shall send the file containing the allocation details to member brokers (Clause 11A.7.12).

(xii) On receipt of the basis of allocation data, the brokers shall immediately intimate the fact of allocation to their client/applicant. The broker shall ensure that each successful client/applicant submits the duly filled in and signed application form to him along with the amount payable towards the application money. Amount already paid by the applicant as margin money shall be adjusted towards the total allocation money payable. The broker shall, thereafter, hand over the application forms of the successful applicants who have paid the application money, to the exchange, which shall submit the same to the Registrar to Issue/company for their records (Clause 11A.7.13).

(xiii) The broker shall refund the margin money collected earlier, within 3 days of receipt of basis of allocation, to the applicants who did not receive allocation (Clause 11A.7.14).

(xiv) The brokers shall give details of the amount received from each client and the names of clients who have not paid the application money to the exchange. The brokers shall also give soft copy of this data of the exchange (Clause 11A.7.15).

(xv) On the pay-in day, the broker shall deposit the amount collected from the clients in the separate bank account opened for primary
issues with the clearing house/bank. The clearing house shall debit the primary issue account of each broker and credit the amount so collected firm each broker to the “Issue Account” (Clause 11A.7.16).

(xvi) In the event of the successful applications failing to pay the application money, the broker through whom such client placed orders, shall bring in the funds to the extent of the client’s default. If the broker does not bring in the funds, he shall be declared as a defaulter by the exchange and action as prescribed under the Bye-Laws of the Stock Exchange shall be initiated against him. In such a case, if the minimum subscription as disclosed in the prospectus is not received, the issue proceeds shall be refunded to the applicants (Clause 11A.7.17).

(xvii) The subscriber shall have an option to receive the security certificates or hold the securities in dematerialised form as specified in the Guidelines (Clause 11A.7.18).

(xviii) The concerned Exchange shall not use the Settlement/Trade Guarantee Fund of the Exchange for honoring brokers commitments in case of failure of broker to bring in the funds (Clause 11A.7.19).

(xix) On payment and receipt of the sum payable on application for the amount towards minimum subscription, the company shall allot the shares to the applicants as per these Guidelines. The Registrar to the issues shall post the share certificates to the investors or, instruct the depository to credit the depository account of each investor, as the case may be (Clause 11A.7.20).

(xx) Allotment of securities shall be made not later than 15 days from the closure of the issue failing which interest at the rate of 15% shall be paid to the investors (Clause 11A.7.21).
(xxi) In cases of applicants who have applied directly or by post to the Registrar to the issue, and have not received allocation, the Registrar to the issue shall arrange to refund the application monies paid by them within the time prescribed (Clause 11A.7.22).

(xxii) The brokers and other intermediaries engaged in the process of offering shares through the on-line system shall maintain the following records for a period of 5 years (Clause 11A.7.23):

- Orders received;
- Applications;
- Details of allocation and allotment;
- Details of margin collected and refunded;
- Details of refund of application money.

(xxiii) SEBI shall have the right to carry out an inspection of the records, books and documents relating to the above, of any intermediary connected with this system and every intermediary in the system shall at all times co-operate with the inspection by SEBI. In addition the stock exchange has the right of supervision and inspection of the activities of its member brokers connected with the system (Clause 11A.7.24).

8. Guidelines for GREEN SHOE OPTION

(A) An issuer company making a public offer of equity shares can avail of the Green Shoe Option (GSO) for stabilizing the post listing price of its shares, subject to the provisions of this Chapter 8A.1. A company desirous of availing the option granted by this Chapter, shall in the resolution of the general meeting authorizing the public issue, seek authorization also for the possibility of allotment of further shares to the ‘stabilizing agent’ (SA) at the end of the stabilization period in terms of clause 8A.15(Clauses 8A.1).
(B) The company shall appoint one of the (merchant bankers or Book Runners, as the case may be, from amongst) the issue management team, as the “stabilizing agent” (SA), who will be responsible for the price stabilization process, if required. The SA shall enter into an agreement with the Issuer Company, prior to filing of offer document with SEBI, clearly stating all the terms and conditions relating to this option including fees charged / expenses to be incurred by SA for this purpose (Clause 8A.2).

(C) The SA shall also enter into an agreement with the promoter(s) or pre issue Shareholders who will lend their shares under the provisions of this Chapter, specifying the maximum number of shares that may be borrowed from the promoters or the shareholders, which shall not be in excess of 15% of the total issue size (Clause 8A.3).

(D) The details of the agreements mentioned in clause 8A.2 and 8A.3 shall be disclosed in 330(the draft prospectus,) the draft Red Herring prospectus, Red Herring prospectus and the final prospectus. The agreements shall also be included as material documents for public inspection in terms of, clause 6.15.1, (Clause 8A.4).

(E) Book Runner Lead Manager, in consultation with the SA, shall determine the amount of shares to be over allotted with the public issue, subject to the maximum number specified in clause 8A.3 (Clause 8A.5).

(F) The (draft prospectus) draft Red Herring prospectus, the Red Herring prospectus and the final prospectus shall contain the following additional disclosures (Clause 8A.6):

a. Name of the SA.

b. The maximum number of shares (as also the percentage vis a
vis the proposed issue size) proposed to be over-allotted by the company.

c. The period, for which the company proposes to avail of the stabilization mechanism.

d. The maximum increase in the capital of the company and the shareholding pattern post issue, in case the company is required to allot further shares to the extent of over-allotment in the issue.

e. The maximum amount of funds to be received by the company in case of further allotment and the use of these additional funds, in final document to be filed with ROC.

f. Details of the agreement/arrangement entered into by SA with the promoters to borrow shares from the latter which inter-alia shall include name of the promoters, their existing shareholding, number & percentage of shares to be lent by them and other important terms and conditions including the rights and obligations of each party.

g. The final prospectus shall additionally disclose the exact number of shares to be allotted pursuant to the public issue, stating separately therein the number of shares to be borrowed from the promoters and over allotted by the SA, and the percentage of such shares in relation to the total issue size.

(G) In case of an initial public offer by a unlisted company, the promoters and pre-issue shareholders and in case of public issue by a listed company, the promoters and pre-issue shareholders holding more than 5% shares, may lend the shares subject to the provisions of this Chapter. The SA shall borrow shares from the promoters or the pre-issue shareholders of the issuer company or both, to the extent of the proposed over-allotment. Provided that
the shares referred to in this clause shall be in dematerialized form only (Clause 8A.7).

(H) The allocation of these shares shall be pro-rata to all the applicants (Clause 8A.8).

(I) The stabilization mechanism shall be available for the period disclosed by the company in the prospectus, which shall not exceed 30 days from the date when trading permission was given by the exchange(s) (Clause 8A.9).

(J) The SA shall open a special account with a bank to be called the “Special Account for GSO proceeds of ______ company” (hereinafter referred to as the GSO Bank account) and a special account for securities with a depository participant to be called the “Special Account for GSO shares of company” (hereinafter referred to as the GSO Demat Account (Clause 8A.10).

(K) The money received from the applicants against the overallotment in the green shoe option shall be kept in the GSO Bank Account, distinct from the issue account and shall be used for the purpose of buying shares from the market, during the stabilization period (Clause 8A.11).

(L) The shares bought from the market by the SA, if any during the stabilization period, shall be credited to the GSO Demat Account (Clause 8A.12).

(M) The shares bought from the market and lying in the GSO Demat Account shall be returned to the promoters immediately, in any case not later than 2 working days after the close of the stabilization period (Clause 8A.13).

(N) The prime responsibility of the SA shall be to stabilize post listing price of the shares. To this end, the SA shall determine the timing of buying the shares, the quantity to be bought, the price at which the shares are to be bought etc (Clause 8A.14).
(O) On expiry of the stabilization period, in case the SA does not buy shares to the extent of shares over-allotted by the company from the market, the issuer company shall allot shares to the extent of the shortfall in dematerialized form to the GSO Demat Account, within five days of the closure of the stabilization period. These shares shall be returned to the promoters by the SA in lieu of the shares borrowed from them and the GSO Demat Account shall be closed thereafter. The company shall make a final listing application in respect of these shares to all the Exchanges where the shares allotted in the public issue are listed. The provisions of Chapter XIII shall not be applicable to such allotment (Clause 8A.15).

(P) The shares returned to the promoters under clause 8A.13 or 8A.15, as the case may be, shall be subject to the remaining lock in period as provided in the proviso the clause 4.14.1(Clauses 8A.16).

(Q) The SA shall remit an amount equal to (further shares allotted by the issuer company to the GSO Demat Account) * (issue price) to the issuer company from the GSO Bank Account. The amount left in this account, if any, after this remittance and deduction of expenses incurred by the SA for the stabilization mechanism, shall be transferred to the investor protection fund(s) of the stock exchange(s) where the shares of Issuer Company are listed, in equal parts if the shares are listed in more than one exchanges. The GSO Bank Account shall be closed soon thereafter (Clause 8A.17).

(R) The SA shall submit a report to the stock exchange(s) on a daily basis during the stabilization period. The SA shall also submit a final report to SEBI in the format specified in Schedule XXIX. This report shall be signed by the SA and the company. This report shall be accompanied with a depository statement for the “GSO Demat Account” for the stabilization period, indicating the flow of
the shares into and from the account. The report shall also be accompanied by an undertaking given by the SA and countersigned by the depository(ies) regarding confirmation of lock-in on the shares returned to the promoters in lieu of the shares borrowed from them for the purpose of the stabilization, as per the requirement specified in 8A.16(Claude 8A.18).

(S) The SA shall maintain a register in respect of each issue having the green shoe option in which he acts as a SA. The register shall contain the following details of:

(a) In respect of each transaction effected in the course of the stabilizing action, the price, date and time.

(b) The details of the promoters from whom the shares are borrowed and the number of shares borrowed from each.

(c) Details of allotments made under clause 8A.15 (Clause 8A.19).

(T) The register must be retained for a period of at least three years from the date of the end of the stabilizing period (Clause 8A.20).

(U) For the purpose of the Chapter VIII-A

(a) Promoter means a promoter as defined in Explanation I to clause 6.4.2.1 of these guidelines.

(b) Over allotment shall mean as an allotment or allocation of shares in excess of the size of a public issue, made by the SA out of shares borrowed from the promoters or the pre-issue shareholders or both, in pursuance of a green shoe option exercised by the company in accordance with the provisions of this Chapter (Clause 8A.21).
SECTION-III
GROWTH OF INDIAN IPO MARKET

IPO market in India has displayed many ups and down during the last two decades. It has observed a sharp rise in the initial years of the liberalized era. The growth observed during the first half of the 90s is mostly credited to the financial liberalization of the economy. Capital market reforms like abolition of the office of controller of capital issues (CCI), constitution of SEBI under the new security and regulation act and relaxation in pricing of capital issues played an important role in such rise.

Table 1.1 shows that IPO market has showed a sharp rise from 692 issues for Rs. 7864 crore during 1993-94 to 1239 IPOs for Rs. 16572 crore during 1994-95. There was a marked decline in the number of IPOs and amount raised through them in 1996-97, mainly as a result of stricter eligibility criteria for public issues imposed by SEBI. The number of IPOs declined to 717 amounting to Rs. 5959 during 1996-97. The number of IPOs further declined in 1997-98 to 52 amounting to Rs1048 crore. The decline in the share of IPOs can be partly attributed to the decline in industrial activity in the country and partly due to strict entry point norms, which disallowed green field projects without track record from accessing the market (Annual Report, SEBI, 1997-98). That’s why, year 1997-98 considered as a part of cold or slump period of Indian IPO market.

For the year 1998-99, only IPOs 18 for Rs. 404 crore were issued. The deficiency of issues of good quality, lack of confidence of investors in new companies and depressed secondary market, were some of the reasons, which slowed down the growth of IPOs (Annual Report, SEBI, 1998-99). There was a recovery in the market the number of IPOs during
## Table 1.1
Growth of Indian IPO Market

<table>
<thead>
<tr>
<th>Year</th>
<th>NO. of IPOs</th>
<th>Amount (in crore Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1993-94</td>
<td>692</td>
<td>7864</td>
</tr>
<tr>
<td>1994-95</td>
<td>1239</td>
<td>16572</td>
</tr>
<tr>
<td>1995-96</td>
<td>1357</td>
<td>10924</td>
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<tr>
<td>1996-97</td>
<td>717</td>
<td>5959</td>
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<td>53</td>
<td>35559</td>
</tr>
<tr>
<td>2011-12</td>
<td>54</td>
<td>41515</td>
</tr>
</tbody>
</table>

Source: Various Annual Reports of SEBI
1999-00 to 51 for Rs. 2719 crore from 18 IPOs for 404 Rs. crore and their successful subscription indicated the restored enthusiasm and confidence of investors to invest in new companies especially in knowledge based industries particularly in information technology and healthcare IPOs (Annual Report, SEBI, 1999-00). This was also a worldwide trend. This tendency continued for 2000-01 when number of IPOs increased to 114 amounting to Rs. 2722 crore. The number again declined to 7 IPOs amounting Rs. 1202 crore during 2001-02. The number of IPOs is very low in 6 and 21 for the year 2002-03 & 2003-04 respectively. In 2004-05 Indian IPO market experienced a boom like situation 23 IPOs collected Rs. 13749 crore. In 2005-06 number of IPOs increased to 79 but amount raised declined to 10936. The momentum witnessed in the primary market as compare to 2005-06 increased in 2006-07.

Strong macro-economic fundamentals, favorable investment climate, encouraging corporate results, and buoyant secondary market performance supported by institutional investors encouraged a number of
companies to raise capital from the primary market (Annual Report, SEBI, 2006-07). Boom also continued for year 2006-07 and 2007-08. In 2006-07 number of IPOs increased to 77 amounting Rs. 28504 crore. The upward trend in primary market activities continued in 2007-08. The buoyancy in the secondary market coupled with strong macro-economic fundamentals, active institutional support led by FIIs and mutual funds encouraged large number of companies to raise resource from the primary market (Annual Report, SEBI, 2007-08).

IPO market touched its leaps and bounds in 2007-08, 85 companies collected Rs. 42595 through their IPOs. The Indian securities markets displayed downward trend in 2008-09. The downswing in the domestic equity markets was in consonance with the downward spiral in global equity markets triggered by the international financial crisis. Sharp fall in the benchmark indices, across the board fall in share prices, decline in market capitalisation, turnover and soaring volatility characterised the stock market behaviour during 2008-09 (Annual Report, SEBI, 2008-09). But, the Indian primary market again remembered its golden era. The continuous growth has observed in Indian IPO market for the year 2009-10, 2010-11, and 2011-12. The number as well as amount raised by IPOs has witnessed a constant expansion during these years.

Indian IPO market has witnessed boom in 1993-94 to 1996-97. But 1997-98 to 2002-03 can be considered as a cold period for Indian primary market. Although, in year 1999-00 and 2000-01 IPO market tried to recover but again failed in 2001-02 & 2002-03. During 2004-05 to 2007-08, again Indian IPO market experienced its golden days. These ups and downs attract the researchers to study the Indian IPO market. The study covered the pricing behavior of IPOs up to 36 months from the date of issue listing, that is why, IPOs issued up to 2007-08 are considered.