CHAPTER - II
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INTRODUCTION

Primarily there are two types of stock markets – the primary market and the secondary market. This is true for the Indian stock markets as well. Basically the primary market is the place where the shares are issued for the first time. So when a company is getting listed for the first time at the stock exchange and issuing shares – this process is undertaken at the primary market. That means the process of the Initial Public Offering or IPO and the debentures are controlled at the primary stock market.

On the other hand the secondary market is the stock market where existing stocks are bought and sold by the retail investors through the brokers. It is the secondary market that controls the price of the stocks. Generally when we speak about investing or trading at the stock market we mean trading at the secondary stock market. It is the secondary market where we can invest and trade in the stocks to get the profit from our stock market investment.

Now these are the broadest classification of the stock markets that is true for any country as well as India. But the Indian stock markets can be divided into further categories depending on various aspects like the mode of operation and the diversification in services. First of the two largest stock exchanges in India can be divided on the basis of operation.

PRIMARY MARKET

Primary Market is also called new issues Market or IPO/FPO market and the Secondary market is called Stock Market.

Figure 1: Classification of Issues

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In the primary market, new issues may be made in five ways namely, public issue, rights issue, Bonus Issue, Preferential issue and private issue.

Public Issue involves sale of securities to members of public either at par or at a premium. Rights Issue involves sale of securities to the existing shareholders/debenture holders at a fixed price.

Bonus Issue is to offer shares to existing shareholders at free of cost. Preferential Issue is an offer of equity by a listed company to a particular or a group of investors at a specific price which may not be related to the existing market price.

Private placement involves selling securities privately to selected investors generally by unlisted companies using the offer document called as inform-motion memorandum.

In the primary market, equity shares, fully convertible debentures (FCD), partially convertible centres (PCD), and non-convertibles debentures (NCD) are the securities commonly issued.

Functions of New Issue Market

The main functions of new issue market are to facilitate transfer of resources from savers to the users. The savers are individuals, commercial banks, insurance companies etc. the users are public limited companies and the government.

The new issue market plays an important role of mobilizing the funds from the savers and transfers them to borrowers for production purposes, an important requisite of economic growth.

It is not only a platform for raising finance to establish new enterprises but also for expansion/diversification/modernizations of existing units. In this basis the new market can be classified as:

1. Market where firms go to the public for the first time through initial public offering (IPO).
2. Market where firms which are already trading to raise additional capital through sea-stoned equity offering (SEO).

The main function of new issue market can be divided into a triple service functions:

1. Origination
2. Underwriting
3. Distribution

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Origation

Origation refers to the work of investigation, analysis and processing of new project proposals. Origation starts before an issue is actually floated in the market. There are two aspects in these functions:

1. A careful study of the technical, economic and financial viability to ensure soundness of the project. This is a preliminary investigation undertaken by the sponsors of the issue.

2. Advisory services which improve the quality of capital issues and ensure its success. The advisory services include:
   - Type of issue: This refers to the kind of securities to be issued whether equity share, preference share, debenture or convertible debenture.
   - Magnitude of issue.
   - Time of floating of an issue.
   - Pricing of an issue – whether shares are to be issued at par or at premium e) Methods of issue.
   - Techniques of selling the securities

The function of origination is done by merchant bankers who may be commercial banks, all Indian financial institutions or private firms. Initially this service was provided by specialized division of commercial banks.

At present, financial institutions and private firms also perform this service. Though this service is highly important, the success of the issue depends, to a large extent, on the efficiency of the market. The origination itself does not guarantee the success of the issue. Underwriting, a specialized service is required in this regard.

Underwriting

Underwriting is an agreement whereby the underwriter promises to subscribe to a specified number of shares or debentures or a specified amount of stock in the event of public not subscribing to the issue. If the issue is fully subscribed then there is no liability for the underwriter. If a part of share issues remain unsold, the underwriter will buy the shares. Thus underwriting is a guarantee for the marketability of shares.

Methods of underwriting

An underwriting agreement may take any of the following three forms:
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1. Standing behind the issue

Under this method, the underwriter guarantees the sale of a specified number of shares within a specified period. If the public do not subscribe to the specified amount of issue, the underwriter buys the balance in the issue.

2. Outright purchase

The Underwriter, in this method, makes outright purchase of shares and resells them to the investors.

3. Consortium method

Underwriting is jointly done by a group of underwriters in this method. The underwriters form a syndicate for this purpose. This method is adopted for large issue.

Advantages of underwriting

Underwriting assumes great significance as it offers the following advantages to the issuing company.

The issuing company is relieved from the risk of finding buyers for the issue offered to the public. The company is assured of raising adequate capital.

The company is assured of getting minimum subscription within the stipulated time, a statutory obligation to be fulfilled by the issuing company.

1. Underwriters undertake the burden of highly specialized function of distributing securities.
2. Provide expert advice with regard to timing of security issue, the pricing of issue, the size and type of securities to be issued etc.
3. Public confidence on the issue enhances when underwritten by reputed underwriters. The underwriters in India may be classified into two categories:

   - Institutional underwriters: The institutional underwriters are
     1. Life Insurance Corporation of India (LIC)
     2. Unit Trust of India (UTI)
     3. Industrial Development Bank of India (IDBI)
     4. Industrial Credit and Investment Corporation of India (ICICI)
     5. Commercial banks and general insurance companies.

   - Non – institutional underwriters.

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The pattern of underwriting of the above institutional underwriters differs vastly in India. LIC and UTI have purchased industrial securities from the new issue market with a view to hold them on their own portfolio. They have a preference for underwriting shares in large and well established firms.

The development banks have given special attention to the issues in back- ward states and industries in the priority list. The thrust of the development banks is also towards small and new issues which do not have adequate support from other institutions. General insurance companies have shown preference in underwriting the securities of fairly new issues.

The non-institutional underwriters are brokers. They guarantee shares only with a view to earn commission from the company floating the issue. They are known to off load the shares later to make a profit.

The brokers work profit motive in underwriting industrial securities. After the elimination of forward trading, stock exchange broker have begun to take an under- written to the total private capital issue varies between 72% to 97%

Distribution

Distribution is the function of sale of securities to ultimate investors. This service is performed by brokers and agents who maintain regular and direct contact with the ultimate investors.

Methods of floating of new issues: The various methods which are used in the floating of securities in the new issue market are:

- Public issues.
- Offer for sale
- Placement
- Rights issues

Public issues

Under this method, the issuing company directly offers to the general public / institutions a fixed number of shares at a stated price through a document called prospectus. This is the most common method followed by joint stock companies to raise capital through the issues of securities.

1. Name of the company
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2. Address of the registered office of the company
3. Existing and proposed activities
4. Location of the industry
5. Names of directors
6. Authorized and proposed issue capital to the public
7. Dates of opening and closing of the subscription list
8. Minimum subscription
10. A statement by the company that it will apply to stock exchange for quotations of its shares.

According to the companies act, 1956 every application form must be accompanied by a pro-spectus. Now, it is no longer necessary to furnish a copy of the prospectus along with every application forms as per the companies Amendment Act, 1988. Now, an abridged prospectus is being annexed to every share application form.

Merits of issue through prospectus

1. Sale through prospectus has the advantage of inviting a large section of the investing public through advertisement
2. It is a direct method and no intermediaries are involved in it.
3. Shares, under this method, are allotted to a large section of investors on a non-discriminatory basis. This procedure helps in wide dispersion of shares and to avoid concentration of wealth in few hands.

Demerits

1. It is an expensive method. The company has to incur expenses on printing of prospectus, advertisement, banks' commission, underwriting commission, legal charges, stamp duty, listing fees and registration charges.
2. This method is suitable only for large issues.

Offer for sale

The method of offer of sale constitute outright sale of securities through the intermediary of issue houses or share brokers. In other words, the shares are not offered to the public directly.

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This method consist of two stages: the first stage is a direct sale by the issuing company to the issue house and brokers at an agreed price. In the second stage, the intermediaries resell the above securities to the ultimate investors.

The issue houses or stock brokers purchase the securities at a negotiated price and resell at a higher price. The difference in the purchase and sale price is called turn or spread.

The advantages of this method are that the company is relieved from the problem of printing and advertisement of prospectus and making allotment of shares. Offer of sale is not common in India. This method is used generally in two instances:

- Offer by a foreign company of a part of it to Indian investors
- Promoters diluting their stake to comply with requirements of stock exchange at the time of listing of shares.

Follow on Public Offering (FPO)

When an existing listed company either makes a fresh issue of securities to the public or makes an offer for sale of securities to the public for the first time, through an offer document, such issues are called ‘Follow on Public Offering’. Such public issue of securities or offer for sale to public is required to satisfy the stock exchange listing obligations along with SEBI guidelines.

Rights Issue (RI)

When a listed company proposes to issue securities to its existing shareholders, whose names appear in the register of members on record date, in the proportion to their existing holding, through an offer document, such issues are called ‘Rights Issue’. This mode of raising capital is best suited when the dilution of controlling interest is not intended.

Preferential Issue

A preferential issue is an issue of equity shares or of convertible securities by listed companies to a select group of persons which is neither a rights issue nor a public issue. The issuer company has to comply with the provisions of the Companies Act, as well as, SEBI’s guidelines with reference to preferential issues as contained in Chapter XIII.

A company which makes any public or rights issue or an offer for sale can issue shares only in dematerialised form. A company shall not make a public or rights issue of shares
unless all the existing partly paid shares have been fully paid-up or forfeited. A company which is making public issue of securities shall make an application to the stock exchange for listing of those shares.

Book Building
It is a capital issuance process which results towards a price discovery and also to assess demand analysis of the security. It is a process used for marketing equity shares of a company.

Book-Building Process involves
- The Issuer nominates a merchant banker as book runner
- Specifies issue size and floor price
- Appoints syndicate members
- Investors place orders into the electronic book, termed as the process of bidding
- Bids are entered, 'at' or 'above' the floor price
- Retail investors can bid at a cut-off price
- The price opted by majority of bidders shall be decided as the subscription price.

Fixed Price vs. Book-Building

<table>
<thead>
<tr>
<th>Fixed Price</th>
<th>Book-Building</th>
</tr>
</thead>
<tbody>
<tr>
<td>Offer price is known to investor</td>
<td>Only the floor price and price in advance range is known</td>
</tr>
<tr>
<td>Demand for the securities known after issue closure</td>
<td>Demand for the securities is visible online as the book is built</td>
</tr>
<tr>
<td>Application money credited to issuer account</td>
<td>Application money is credited to an escrow account</td>
</tr>
</tbody>
</table>

Table 1: Fixed Price vs. Book-Building
Source: NSE-India.com
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Figure 2: Bidding Process
Price Discovery Process

With Illustrative Numbers

Cumulative Day 1 Demand

<table>
<thead>
<tr>
<th>Demand (Cost Shares)</th>
<th>115</th>
<th>120</th>
<th>125</th>
<th>130</th>
<th>135</th>
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<tr>
<td>Price (Rs/share)</td>
<td>100</td>
<td>80</td>
<td>60</td>
<td>40</td>
<td>20</td>
</tr>
</tbody>
</table>

Last Day Demand

<table>
<thead>
<tr>
<th>Demand (Cost Shares)</th>
<th>115</th>
<th>120</th>
<th>125</th>
<th>130</th>
<th>135</th>
</tr>
</thead>
<tbody>
<tr>
<td>Price (Rs/share)</td>
<td>250</td>
<td>200</td>
<td>150</td>
<td>100</td>
<td>50</td>
</tr>
</tbody>
</table>

Total Daily Demand

<table>
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<tr>
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<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
</tr>
</thead>
<tbody>
<tr>
<td>Day</td>
<td>250</td>
<td>200</td>
<td>150</td>
<td>100</td>
<td>50</td>
</tr>
</tbody>
</table>

Investors have an option to revise their bids till Book Closure

Book is open for 6 days

Figure 3: Price Discovery Process
Eligibility Norms for Public Issue

SEBI has laid down the eligibility norms for entities accessing the primary market through public issues. The entry norms for companies making initial public offer or Follow on Public offer, are summarised as follows (students are advised to refer to SEBI guidelines to have the latest norms):

**Entry Norm I**

The company shall meet the following requirements:

(a) Net tangible assets of at least Rs. 3 cores for 3 full years.

(b) Distributable profits in at least three years.

(c) Net worth of at least Rs. 1 core in three years.

(d) If change in name, at least 50% revenue for preceding 1 year should be from the new active- it.

(e) The issue size does not exceed 5 times the pre-issue net worth.

To provide sufficient flexibility and also to ensure that genuine companies do not suffer on account of rigidity of the parameters, SEBI has provided two other alternative routes to companies not satisfying any of the above conditions, for accessing the primary market.

**Entry Norm II**

Issue shall be through book building route, with at least 50% to be mandatorily allotted to the Qualified Institutional Buyers (QIBs).

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

**OR**

**Entry Norm III**

a) The 'project' is appraised and participated to the extent of 15% by FIs/Scheduled com- mer- coal banks of which at least 10% comes from the appraiser(s).
b) The minimum post-issue face value capital shall be Rs. 10 cores or there shall be a compulsory market-making for at least 2 years in addition to satisfying the aforesaid eligibility norms, the company shall also satisfy the criteria of having at least 1000 prospective allottees in its issue.

Green Shoe Option

Green Shoe Option denotes 'an option of allocating shares in excess of the shares included in the public issue'. It is an option allowing the Issuing Company to issue additional shares when the demand is high for the shares when the flotation is on. SEBI guidelines allows the Issuing company to accept oversubscription, subject to a ceiling, say 15% of the offer made to public. In certain cases, the Green Shoe Option can be even more than 15%. It is extensively used in international IPOs to stabilise the post listing price of new issued shares. The concept has been introduced in the Indian capital market and is used in initial public offerings through book building process. SEBI has allowed the use of the option with a view to boost the investors' confidence and to put a check for speculative practices causing short-term volatility in post listing price. The Green Shoe Option facility would bring in price stability of initial public offerings.

Kinds of Offer Document

An offer document means 'prospectus' in case of a public issue or an offer for sale and 'Letter of offer' in case of rights issue, which is required to be filed with the Registrar of Companies (ROC) and Stock Exchanges. An offer document covers all the relevant informal-in to help an investor in making wise investment decisions.

Draft Prospectus - A company before making any public issue of securities shall file a draft prospectus with SEBI, through an eligible merchant banker, at least 21 days prior to the filing of prospectus with the Registrar of Companies. If any specific changes are suggested by SEBI within the said 21 days, the Issuing company or the lead merchant banker shall carryout such changes in the draft prospectus before filing the prospectus with ROC.

Draft Letter of Offer - A listed company, before making any rights issue for an amount exceeding Rs. 50 laths (including premium) shall file a draft letter of offer with SEBI, at least

21 days prior to the filing of the letter of offer with regional stock exchange and shall carry changes as suggested by SEBI before the filing of the draft letter of offer with regional stock exchange.
Prospectus - A company issuing shares to public must issue a 'prospectus'. The prospectus is an 'invitation' to offer. It is an invitation to the public to take shares or debentures in the company or deposit money in the company. Section 2(36) of the Companies Act, 1956 defines prospectus as "any document described or issued as a prospectus and includes any notice, circular, advertisement or other document inviting deposits from the public or invite-in offers from the public for the subscription or purchase of any shares in, or debentures of, a body corporate". Section 56 of the Companies Act provides that every prospectus must disclose matters specified in Schedule II.

Abridged Prospectus - Section 2(1) of the Companies Act, 1956 defines abridged prospectus means 'a memorandum containing such salient features of a prospectus as may be prescribed'. An abridged prospectus means the memorandum as prescribed in Form 2A under sub-section (3) of section 56 of the Companies Act. It contains all the salient features of a prospectus. A company cannot supply application forms for shares or debentures unless the form is carom-pained by abridged prospectus.

Shelf Prospectus - Sometimes, securities are issued in stages spread over a period of time, particularly in respect of infrastructure projects where issue size is large as huge funds have to be collected. In such cases, filing of prospectus each time will be very expensive. In such cases, section 60A of the Companies Act, 1956 allows a prospectus called 'Shelf Prospectus' to be filed with Registrar of Companies. At subsequent stages only 'Information Memorandum' is required to be filed. The shelf prospectus shall be valid for a period of 1 year from the date of opening of first issue of securities under that prospectus.

Information Memorandum - The Information Memorandum shall contain all material facts relating to new charges created, changes in the financial position as have accrued between the first offer, previous offer and the succeeding offer. The Information Memorandum shall be filed with a period of 3 months prior to making of second or subsequent offer of securities under Shelf Prospectus. The Information Memorandum shall be issued to the public along with Shelf Prospectus filed at the first stage of offer. Where an update of Information Memo-random is filed every time an offer of securities is made, such memorandum together with the Shelf Prospectus shall constitute the Prospectus.

Red-Herring Prospectus: A prospectus is said to be a red-herring prospectus which contains all information as per prospectus contents but does not have information on price of securities offered and number of securities (quantum) offered through such document. Thus, a red-her-ring prospectus lacks price and quantity of the securities offered. This is used in book building. Issues only. In the case of book built issues, it is a
process of price discovery and the price cannot be determined until bidding process is completed. Hence, such details are not shown in Red-herring prospectus filed with ROC in terms of the provisions of the Companies Act. Only on completion of the bidding process, the details of the final price are included in the offer document. The offer document filed thereafter with ROC is called a 'prospectus'.

Disadvantages of Floatation

- The disadvantages of flotation include the following:
- There are considerable costs in flotation and listing.
- It takes lot of management's time, before and after flotation and listing.
- The company must comply with the stringent stock exchange regulations.
- It will be necessary to meet the regulatory requirements for disclosure of information, including details of managerial remuneration.
- A dilution of management control will result from the widely held shares of the company.
- The affairs of the company are subject to public scrutiny and fluctuations in share price may sometime cause adverse image in the public.
- Since the costs of flotation are higher, other ways of raising finance would reduce the cost of funds.
- Listed company status will put additional burden on the managerial staff.
- The buying and selling of shares by the directors and other related persons may attract the provisions of 'insider trading'.
- There will always be pressure from shareholders to declare dividends, which may not be in the interests of the company.
- The adverse campaigns against the company may drive down the share price; it is technically called 'bear raids'.
- The investors always expect the rise in the share price. The company's growth and profit-ability may not afford the increase in share price always.
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Promoters

The 'promoter' has been defined as a person or group of persons who are instrumental in formation of the company, who enable the company to start its commercial operations by bringing in the necessary funds required for the concern. The promoters are in the overall control of the company, whose names are mentioned in the offer document. Any director or officer discharging their functions in their professional capacity cannot be termed as promoter. The meaning of the term 'promoter' is wide enough to cover the following relationships:

- 'Promoter group' includes promoter, an immediate relative of the promoter (i.e. any spouse of that person, or any parent, brother, sister or child of the person or of the spouse).
- In case promoter is a company, a subsidiary or holding company of that company.
- Any company in which the promoter holds 10% or more of the equity capital or which holds 10% or more of the equity capital of the promoter.
- Any company in which a group of individuals or companies or combinations thereof who holds 20% or more of the equity capital in that company, also holds 20% or more of the equity capital of the issuer company.
- In case the promoter is an individual, any company in which 10% or more of the share capital is held by the promoter or an immediate relative of the promoter or a firm or HUF in which the promoter or any one or more of his immediate relative is a member.

Promoter Contribution

- Promoter's contribution in any public issue shall be in accordance with the following provisions under SEBI's Guidelines:
  - Unlisted companies - In the public issue, the promoters shall contribute not less than 20% of the post issue capital.
  - Offers for sale - The promoters share holding after offer for sale shall not be less than 20% of post issue capital.
  - Listed companies - The promoters shall participate either to the extent of 20% of the pro- posed issue or ensure post-issue shareholding to the extent of 20% of the post-issue capital.
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- Composite issues of listed companies - The promoters contribution shall at the option of the promoters be either 20% of the proposed public issue or 20% of the post issue capital. Rights issue component of the composite issue shall be excluded while calculating the post issue capital.

Regulatory Frame Work

SEBI DIP Guidelines now got replaced with ICDR guidelines. The Salient features of the Regulatory Frame Work and Salient Features of the same as contained in Chapter-I to Chapter-V of ICDR Regulations are encapsulated hereunder:

SEBI REGULATIONS, 2009

These regulations may be called the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2009. They came into force on the date of their publication in the Official Gazette on 26th August, 2009.

CHAPTER-I PRELIMINARY

Short title and commencement.

1. (1) These regulations may be called the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2009.

(2) They shall come into force on the date of their publication in the Official Gazette.

Definitions.

2. (1) In these regulations, unless the context otherwise requires:

(a) "Act" means the Securities and Exchange Board of India Act, 1992 (15 of 1992);

(b) "advertisement" includes notices, brochures, pamphlets, show cards, catalogues, hoardings, placards, posters, insertions in newspaper, cover pages of offer documents, pictures and films in any print media or electronic media, radio, television programme;

(c) "anchor investor" means a qualified institutional buyer¹ [who makes] an application for a value of ten crore rupees or more in a public issue made through the book building process in accordance with these regulations;

¹ Substituted by SEBI (Issue of Capital and Disclosure Requirements) (Amendment) Regulations, 2009, w.e.f.

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(d) "Application Supported by Blocked Amount (ASBA)" means an application for subscribing to a public issue or rights issue, along with an authorisation to Self-Certified Syndicate Bank to block the application money in a bank account;

(e) "Board" means the Securities and Exchange Board of India established under section 3 of the Act;

(f) "book building" means a process undertaken to elicit demand and to assess the price for determination of the quantum or value of specified securities or Indian Depository Receipts, as the case may be, in accordance with these regulations;

(g) "book runner" means a merchant banker appointed by the issuer to undertake the book building process;

(h) "composite issue" means an issue of specified securities by a listed issuer on public- cum-rights basis, wherein the allotment in both public issue and rights issue is proposed to be made simultaneously;

(i) "control" shall have the same meaning as assigned to it under clause (c) of sub-regulation (1) of regulation 2 of the Securities and Exchange Board of India (Substantial Acquisitions of Shares and Takeovers) Regulations, 1997;

(j) "convertible debt instrument" means an instrument which creates or acknowledges indebtedness and is convertible into equity shares of the issuer at a later date at or without the option of the holder of the instrument, whether constituting a charge on the assets of the issuer or not;

(k) 2 ["convertible security" means a security which is convertible into or exchangeable with equity shares of the issuer at a later date, with or without the option of the holder of the security and includes convertible debt instrument and convertible preference shares;]

(l) "designated stock exchange" means a recognised stock exchange in which securities of an issuer are listed or proposed to be listed and which is chosen by the issuer as a designated

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11.12.2009, Prior to its substitution, clause (k) read as under:

"(k) "convertible security" means a security which is convertible into or exchangeable with equity shares of the issuer at a later date with or without the option of the holder of the security and includes convertible debt instrument;"

2 Substituted by SEBI (Issue of Capital and Disclosure Requirements) (Third Amendment) Regulations, 2010, w.e.f. 13.04.2010. Prior to its substitution, clause (m) read as under: "(m) "Employee" means a permanent and full-time employee of the issuer, working in India or abroad or a director of the issuer, whether whole time or part time and does not include promoters and an immediate relative of the promoter (i.e., any spouse of that person, or any parent, brother, sister or child of the person or of the spouse);"
stock exchange for the purpose of a particular issue of specified securities under these regulations:

Provided that where one or more of such stock exchanges have nationwide trading terminals, the issuer shall choose one of them as the designated stock exchange:

Provided further that subject to the provisions of this clause, the issuer may choose a different recognised stock exchange as a designated stock exchange for any subsequent issue of specified securities under these regulations;

(m) 3("employee" means a permanent and full-time employee, working in India or abroad, of the issuer or of the holding company or subsidiary company or of that material associate(s) of the issuer whose financial statements are consolidated with the issuer’s financial statements as per Accounting Standard 21, or a director of the issuer, whether whole time or part time and does not include promoters and an immediate relative of the promoter (i.e., any spouse of that person, or any parent, brother, sister or child of that person or of the spouse);

(n) “further public offer” means an offer of specified securities by a listed issuer to the public for subscription and includes an offer for sale of specified securities to the public by any existing holders of such securities in a listed issuer;

(o) “green shoe option” means an option of allotting equity shares in excess of the equity shares offered in the public issue as a post-listing price stabilizing mechanism;

(p) “initial public offer” means an offer of specified securities by an unlisted issuer to the public for subscription and includes an offer for sale of specified securities to the public by any existing holders of such securities in an unlisted issuer;

(q) “issue size” includes offer through offer document and promoters’ contribution;

(r) “issuer” means any person making an offer of specified securities;

(s) “key management personnel” means the officers vested with executive powers and the officers at the level immediately below the board of directors of the issuer and includes any other person whom the issuer may declare as a key management personnel;

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3 Substituted by SEBI (Issue of Capital and Disclosure Requirements) (Third Amendment) Regulations, 2010, w.e.f. 13.04.2010. Prior to its substitution, clause (m) read as under:

“(m) “employee” means a permanent and full-time employee of the issuer, working in India or abroad or a director of the issuer, whether whole time or part time and does not include promoters and an immediate relative of the promoter (i.e., any spouse of that person, or any parent, brother, sister or child of the person or of the spouse);”

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(t) "listed issuer" means an issuer whose equity shares are listed in a recognised stock exchange;

(u) "net offer to public" means an offer of specified securities to the public but does not include reservations;

(v) "net worth" means the aggregate of the paid up share capital, share premium account, and reserves and surplus (excluding revaluation reserve) as reduced by the aggregate of miscellaneous expenditure (to the extent not adjusted or written off) and the debit balance of the profit and loss account;

(w) "non-institutional investor" means an investor other than a retail individual investor and qualified institutional buyer;

(x) "offer document" means a red herring prospectus, prospectus or shelf prospectus and information memorandum in terms of section 60A of the Companies Act, 1956 in case of a public issue and letter of offer in case of a rights issue;

(y) "offer through offer document" means net offer to public and reservations;

(z) "preferential issue" means an issue of specified securities by a listed issuer to any select person or group of persons on a private placement basis and does not include an offer of specified securities made through a public issue, rights issue, bonus issue, employee stock option scheme, employee stock purchase scheme or qualified institutions placement or an issue of sweat equity shares or depository receipts issued in a country outside India or foreign securities;

(za) "promoter" includes:

(i) the person or persons who are in control of the issuer;

(ii) the person or persons who are instrumental in the formulation of a plan or programme pursuant to which specified securities are offered to public;

(iii) the person or persons named in the offer document as promoters:

Provided that a director or officer of the issuer or a person, if acting as such merely in his professional capacity, shall not be deemed as a promoter:

Provided further that a financial institution, scheduled bank, foreign institutional investor and mutual fund shall not be deemed to be a promoter merely by virtue of the fact that ten per cent. or more of the equity share capital of the issuer is held by such person;
Provided further that such financial institution, scheduled bank and foreign institutional investor shall be treated as promoter for the subsidiaries or companies promoted by them or for the mutual fund sponsored by them;

(zb) "promoter group" includes: (i) the promoter;

(ii) an immediate relative of the promoter (i.e., any spouse of that person, or any parent, brother, sister or child of the person or of the spouse); and

(iii) in case promoter is a body corporate:

(A) a subsidiary or holding company of such body corporate;

(B) anybody corporate in which the promoter holds ten per cent. or more of the equity share capital or which holds ten per cent. or more of the equity share capital of the promoter;

(C) anybody corporate in which a group of individuals or companies or combinations thereof which hold twenty per cent. or more of the equity share capital in that body corporate also holds twenty per cent. or more of the equity share capital of the issuer; and

(iv) in case the promoter is an individual:

(A) anybody corporate in which ten per cent. or more of the equity share capital is held by the promoter or an immediate relative of the promoter or a firm or Hindu Undivided Family in which the promoter or any one or more of his immediate relative is a member;

(B) anybody corporate in which a body corporate as provided in (A) above holds ten per cent. or more, of the equity share capital;

(C) any Hindu Undivided Family or firm in which the aggregate shareholding of the promoter and his immediate relatives is equal to or more than ten per cent. of the total; and

(v) all persons whose shareholding is aggregated for the purpose of disclosing in the prospectus under the heading "shareholding of the promoter group":

Provided that a financial institution, scheduled bank, foreign institutional investor and mutual fund shall not be deemed to be promoter group merely by virtue of the fact that ten per cent. or more of the equity share capital of the issuer is held by such person: Provided further that such financial institution, scheduled bank and foreign institutional investor shall be treated as promoter group for the subsidiaries or companies promoted by them or for the mutual fund sponsored by them;
(zc) "public issue" means an initial public offer or further public offer; (zd) "qualified institutional buyer" means:

(i) a mutual fund, venture capital fund and foreign venture capital investor registered with the Board;

(ii) a foreign institutional investor and sub-account (other than a sub-account which is a foreign corporate or foreign individual), registered with the Board;

(iii) a public financial institution as defined in section 4A of the Companies Act, 1956; (iv) a scheduled commercial bank;

(v) a multilateral and bilateral development financial institution; (vi) a state industrial development corporation;

(vii) an insurance company registered with the Insurance Regulatory and Development Authority;

(viii) a provident fund with minimum corpus of twenty five crore rupees; (ix) a pension fund with minimum corpus of twenty five crore rupees;


4[(xi) insurance funds set up and managed by army, navy or air force of the Union of India;]

5[(xii) insurance funds set up and managed by the Department of Posts, India;]

(ze) "retail individual investor" means an investor who applies or bids for specified securities for a value of not more than 6[two lakhs] rupees;

(zf) "retail individual shareholder" means a shareholder of a listed issuer, who:

(i) 7[***]
(ii) applies or bids for specified securities for a value of not more than [two lakhs] rupees;

(zg) "rights issue" means an offer of specified securities by a listed issuer to the shareholders of the issuer as on the record date fixed for the said purpose;

(zh) "Schedule" means schedule annexed to these regulations;

(zi) "Self Certified Syndicate Bank" means a banker to an issue registered with the Board, which offers the facility of Application Supported by Blocked Amount;

(zj) "specified securities" means equity shares and convertible securities;

(zk) "stabilising agent" means a merchant banker who is responsible for stabilising the price of equity shares under a green shoe option, in terms of these regulations;

(zl) "syndicate member" means an intermediary registered with the Board and who is permitted to carry on the activity as an underwriter;

(zm) "unlisted issuer" means an issuer which is not a listed issuer.

(2) All other words and expressions used but not defined in these regulations, but defined in the Act or the Companies Act, 1956, the Securities Contracts (Regulation) Act, 1956, the Depositories Act, 1996 and/or the rules and regulations made there under shall have the same meaning as respectively assigned to them in such Acts or rules or regulations or any statutory modification or re-enactment thereto, as the case may be.

Applicability of the regulations

3. Unless otherwise provided, these regulations shall apply to the following:

a) A public issue;

b) A rights issue, where the aggregate value of specified securities offered is fifty lakh rupees or more;

c) A preferential issue;

"(i) as on the date fixed for the purpose of determining shareholders eligible for reservation in terms of regulation 42 of these regulations, is holding equity shares which, on the basis of the closing price of the equity shares on the recognised stock exchange in which highest trading volume in respect of the equity shares of the issuer was recorded as on the previous day, are worth up to one lakh rupees; and"
d) An issue of bonus shares by a listed issuer;

e) A qualified institutions placement by a listed issuer; (f) an issue of Indian Depository Receipts 9(1) 10(Provided that the provisions of these regulations shall not apply to issue of securities under clause (b), (d) and (e) of sub-regulation (1) of regulation 9 of Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011.)

CHAPTER II - COMMON CONDITIONS FOR PUBLIC ISSUES AND RIGHTS ISSUES

General conditions

4. (1) Any issuer offering specified securities through a public issue or rights issue shall satisfy the conditions of this Chapter at the time of filing draft offer document with the Board (unless stated otherwise in this Chapter) and at the time of registering or filing the final offer document with the Registrar of Companies or designated stock exchange, as the case may be.

(2) No issuer shall make a public issue or rights issue of specified securities:

a) If the issuer, any of its promoters, promoter group or directors or persons in control of the issuer are debarred from accessing the capital market by the Board;

b) If any of the promoters, directors or persons in control of the issuer was or also is a promoter, director or person in control of any other company which is debarred from accessing the capital market under any order or directions made by the Board;

c) If the issuer of convertible debt instruments is in the list of wilful defaulters published by the Reserve Bank of India or it is in default of payment of interest or repayment of principal amount in respect of debt instruments issued by it to the public, if any, for a period of more than six months;

d) Unless it has made an application to one or more recognised stock exchanges for listing of specified securities on such stock exchanges and has chosen one of them as the designated stock exchange: Provided that in case of an initial public offer, the issuer shall make an application for listing of the specified securities in at least one recognised stock exchange having nationwide trading terminals;

e) Unless it has entered into an agreement with a depository for dematerialisation of specified securities already issued or proposed to be issued;

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f) Unless all existing partly paid-up equity shares of the issuer have either been fully paid up or forfeited;

g) Unless firm arrangements of finance through verifiable means towards seventy five per cent. of the stated means of finance, excluding the amount to be raised through the proposed public issue or rights issue or through existing identifiable internal accruals, have been made. 8[(3) Warrants may be issued along with public issue or rights issue of specified securities subject to the following:

a) The tenure of such warrants shall not exceed twelve months from their date of allotment in the public/rights issue;

b) Not more than one warrant shall be attached to one specified security.]

Appointment of merchant banker and other intermediaries

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

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

(3) Where the issue is managed by more than one merchant banker, the rights, obligations and responsibilities, relating inter alia to disclosures, allotment, refund and underwriting obligations, if

(4) The lead merchant banker shall, only after independently assessing the capability of other intermediaries to carry out their obligations, advise the issuer on their appointment.

(5) The issuer shall enter into an agreement with the lead merchant banker in the format specified in Schedule II and with other intermediaries as required under the respective regulations applicable to the intermediary concerned: Provided that such agreements may include such other clauses as the issuer and the intermediary may deem fit without diminishing or limiting in any way the liabilities and obligations of the merchant bankers, other

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8 Inserted by SEBI (Issue of Capital and Disclosure Requirements) (Amendment) Regulations, 2012, w.e.f. 30.01.2012. any, of each merchant banker shall be predetermined and disclosed in the offer document as specified in Schedule I.
intermediaries and the issuer under the Act, the Companies Act, 1956, the Securities Contracts (Regulation) Act, 1956, the Depositories Act, 1996 and the rules and regulations made there under or any statutory modification or statutory enactment thereof: Provided further that in case of ASBA process, the issuer shall take cognisance of the deemed agreement of the issuer with Self Certified Syndicate Banks.

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

(7) The issuer shall appoint a registrar which has connectivity with all the depositories: Provided that if issuer itself is a registrar to an issue registered with the Board, then another registrar to an issue shall be appointed as registrar to the issue: Provided further that the lead merchant banker shall not act as a registrar to the issue in which it is also handling the post issue responsibilities.

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

Filing of offer document

6. (1) No issuer shall make,

   a) A public issue; or

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

(2) The Board may specify changes or issue observations, if any, on the draft offer document within thirty days from the later of the following dates:

   a) The date of receipt of the draft offer document under sub-regulation (1); or

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

   c) The date of receipt of clarification or information from any regulator or agency, where the Board has sought any clarification or information from such regulator or agency; or
d) The date of receipt of a copy of in-principle approval letter issued by the recognised
stock exchanges.

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

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

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

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

In-principle approval from recognised stock exchanges

7. The issuer shall obtain in-principle approval from recognised stock exchanges as follows:

a) In case of an initial public offer, from all the recognised stock exchanges in which the
issuer proposes to get its specified securities listed; and

b) In case of a further public offer and rights issue:

I. Where the specified securities are listed only on recognised stock exchanges having
nationwide trading terminals, from all such stock exchanges;

II. Where the specified securities are not listed on any recognised stock exchange
having nationwide trading terminals, from all the stock exchanges in which the
specified securities of the issuer are proposed to be listed;

III. Where the specified securities are listed on recognised stock exchanges
having nationwide trading terminals as well as on the recognised stock exchanges
not having nationwide trading terminals, from all recognised stock exchanges having
nationwide trading terminals.
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Documents to be submitted before opening of the issue

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

9[(a) a certificate, confirming that an agreement has been entered into between the issuer and The lead merchant bankers as per the format specified in Schedule II.]

(b) [**]

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

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

[(e) a certificate confirming compliance of the conditions specified in Part C of Schedule VIII.]

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

a) A statement certifying that all changes, suggestions and observations made by the Board have been incorporated in the offer document;

b) A due diligence certificate as per Form C of Schedule VI, at the time of registering the prospectus with the Registrar of Companies;

c) A copy of the resolution passed by the board of directors of the issuer for allotting specified securities to promoters towards amount received against promoters' contribution, before opening of the issue;

d) A certificate from a Chartered Accountant, before opening of the issue, certifying that promoters' contribution has been received in accordance with these regulations,

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9 Substituted by SEBI (Issue of Capital and Disclosure Requirements) (Amendment) Regulations, 2012, w.e.f. 30.01.2012. Prior to its substitution, clause (a) read as under.
"(a) a copy of the agreement entered into between the issuer and the lead merchant bankers;"

10 Clause (b) omitted by SEBI (Issue of Capital and Disclosure Requirements) (Amendment) Regulations, 2012, w.e.f. 30.01.2012. Prior to its omission, clause (b) read as under:
"(b) a copy of inter-se allocation of responsibilities of each merchant banker, in case the issue is managed by more than one merchant banker;"

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accompanying therewith the names and addresses of the promoters who have contributed to the promoters' contribution and the amount paid by each of them towards such contribution;

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

f) A due diligence certificate as per Form E of Schedule VI, after the issue has opened but before it closes for subscription.

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

Draft offer document to be made public.

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

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

11[(3) the issuer either on the date of filing the draft offer document with the Board or on the next day shall make a public announcement in one English national daily newspaper with wide circulation, one Hindi national daily newspaper with wide circulation and one regional language newspaper with wide circulation at the place where the registered office of the issuer is situated, disclosing to the public the fact of filing of draft offer document with the Board and inviting the public to give their comments to the Board in respect of disclosures made in the draft offer document.]

Fast Track Issue

10. (1) nothing contained in sub-regulations (1), (2) and (3) of regulation 6 and regulations 7 and 8 shall apply to a public issue or rights issue if the issuer satisfies the following conditions:

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11 Inserted by the SEBI (Issue of Capital and Disclosure Requirements) (Fourth Amendment) Regulations, 2010, w.e.f. 12.11.2010.

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a) The equity shares of the issuer have been listed on any recognised stock exchange having nationwide trading terminals for a period of at least three years immediately preceding the reference date;

b) The average market capitalisation of public shareholding of the issuer is at least 16[five Thousand crore rupees];

c) The annualised trading turnover of the equity shares of the issuer during six calendar months immediately preceding the month of the reference date has been at least two per cent. Of the weighted average number of equity shares listed during such six months' period: 17[Provided that for issuers, whose public shareholding is less than fifteen per cent. of its issued equity capital, the annualised trading turnover of its equity shares has been at least two per cent. Of the weighted average number of equity shares available as free float during such six months' period;]

d) The issuer has redressed at least ninety five per cent. Of the complaints received from the investors till the end of the quarter immediately preceding the month of the reference dates;

e) The issuer has been in compliance with the equity listing agreement for a period of at least three years immediately preceding the reference date: 18[Provided that if the issuer has not complied with the provision of the equity listing agreement relating to composition of board of directors, for any quarter during the last three years immediately preceding the reference date, but is compliant with such provisions at the time of filing of offer document with the Registrar of Companies or designated stock exchange, as the case may be, and adequate disclosures are made in the offer document about such non-compliances during the three years immediately preceding the reference date, it shall be deemed as compliance with the condition;]

f) The impact of auditors' qualifications, if any, on the audited accounts of the issuer in respect of those financial years for which such accounts are disclosed in the offer document does not exceed five per cent. Of the net profit or loss after tax of the issuer for the respective years;

g) No show-cause notices have been issued or prosecution proceedings initiated 19[by the Board] or pending against the issuer or its promoters or whole time directors as on the reference date;

h) The entire shareholding of the promoter group of the issuer is held in dematerialised form on the reference date.
(2) The issuer shall file the offer document with the Board and the recognised stock exchanges in accordance with sub-regulations (4), (5) and (6) of regulation 6 and shall pay fees to the Board as specified in Schedule IV.

(3) The lead merchant bankers shall submit to the Board, the following documents along with the offer document:

a) A due diligence certificate as per Form A of Schedule VI including additional confirmations as specified in Form F of Schedule VI;

b) In case of a fast track issue of convertible debt instruments, a due diligence certificate from the debenture trustee as per Form B of Schedule VI.

Explanation: For the purposes of this regulation:

(I) "reference date" means:

a) In case of a public issue by a listed issuer, the date of registering the red herring prospectus (in case of a book built issue) or prospectus (in case of a fixed price issue) with the Registrar of Companies; and

b) In case of a rights issue by a listed issuer, the date of filing the letter of offer with the designated stock exchange.

(II) "average market capitalisation of public shareholding" means 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 shareholders or the board of the issuer, as the case may be, divided by the number of trading days.

(III) "Public shareholding" shall have the same meaning as assigned to it in the equity listing agreement.

Opening of an issue.

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

a) Within twelve months from the date of issuance of the observations by the Board under regulation 8; or

b) Within three months of expiry of the period stipulated in sub-regulation (2) of regulation 6, if the Board has not issued observations: Provided that in case of a fast
track issue, the issue shall open within the period stipulated in sub-section (4) of section 60 of the Companies Act, 1956.

(2) In case of shelf prospectus, the first issue may be opened within three months of issuance of observations by the Board.

(3) The issuer shall, before registering the red herring prospectus (in case of a book built issue) or prospectus (in case of a fixed price issue) with the Registrar of Companies or filing the letter of offer with the designated stock exchange, as the case may be, file with the Board through the lead merchant bankers, an updated offer document highlighting all changes made in the offer document. (4) Notwithstanding anything contained in this regulation, if there are changes in the offer document in relation to the matters specified in Schedule VII, the updated offer document or new draft offer document, as the case may be, shall be filed with the Board along with fees specified in Schedule IV.

Dispatch of issue material.

12. The lead merchant bankers shall dispatch the offer document and other issue material including forms for ASBA to the designated stock exchange, syndicate members, underwriters, and bankers to the issue, investors' associations and Self Certified Syndicate Banks in advance.

Underwriting

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

(2) Where the issuer makes a public issue through the book building process, such issue shall be underwritten by book runners or syndicate members: 20[Provided that at least fifty per cent. of the net offer to the public proposed to be compulsorily Allotted to qualified institutional buyers for the purpose of compliance of the eligibility conditions specified in sub-regulation (2) of regulation 26 and regulation 27, cannot be underwritten.]

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

(4) If syndicate members fail to fulfil their underwriting obligations, the lead book runner shall fulfil the underwriting obligations.
(5) The book runners and syndicate members shall not subscribe to the issue in any manner except for fulfilling their underwriting obligations.

(6) [***]

(7) In case of every underwritten issue, the lead merchant banker or the lead book runner shall undertake minimum underwriting obligations as specified in the Securities and Exchange Board of India (Merchant Bankers) Regulations, 1992.

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

**Minimum subscription**

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

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

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

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

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

(4) Nothing contained in this regulation shall apply to:

(a) offer for sale of specified securities;

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

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

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Oversubscription

15. No allotment shall be made by the issuer in excess of the specified securities offered through the offer document: Provided that in case of oversubscription, an allotment of not more than ten per cent. Of the net offer to public may be made for the purpose of making allotment in minimum lots.

Monitoring agency

16. (1) If the issue size exceeds five hundred crore rupees, the issuer shall make arrangements for the use of proceeds of the issue to be monitored by a public financial institution or by one of the scheduled commercial banks named in the offer document as bankers of the issuer: Provided that nothing contained in this clause shall apply to an offer for sale or an issue of specified securities made by a bank or public financial institution [or an insurance company].

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

Manner of calls

17. If the issuer proposes to receive subscription monies in calls, it shall ensure that the outstanding subscription money is called within twelve months from the date of allotment in the issue and if any applicant fails to pay the call money within the said twelve months, the equity shares on which there are calls in arrear along with the subscription money already paid on such shares shall be forfeited: Provided that it shall not be necessary to call the outstanding subscription money within twelve months, if the issuer has appointed a monitoring agency in terms of regulation 16.

Allotment, refund and payment of interest

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

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

Restriction on further capital issues

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

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

b) In case of other issues, during the period between the date of filing the draft offer document with the Board and the listing of the specified securities offered through the offer document or refund of application moneys; Unless full disclosures regarding the total number of specified securities and amount proposed to be raised from such further issue are made in such draft offer document or offer document, as the case may be.

Additional requirements for issue of convertible debt instruments

20. (1) In addition to other requirements laid down in these regulations, an issuer making a public issue or rights issue of convertible debt instruments shall comply with the following conditions:

a) It has obtained credit rating from one or more credit rating agencies;

b) It has appointed one or more debenture trustees in accordance with the provisions of section 117B of the Companies Act, 1956 and Securities and Exchange Board of India (Debenture Trustees) Regulations, 1993;

c) It has created debenture redemption reserve in accordance with the provisions of section 117C of the Companies Act, 1956;

d) If the issuer proposes to create a charge or security on its assets in respect of secured convertible debt instruments, it shall ensure that:

I. Such assets are sufficient to discharge the principal amount at all times; (ii) such assets are free from any encumbrance;

II. Where security is already created on such assets in favour of financial institutions or banks or the issue of convertible debt instruments is proposed to be secured by creation of security on a leasehold land, the consent of such financial institution, bank or lesser for a second or pari passu charge has been obtained and submitted to the debenture trustee before the opening of the issue;

Researcher: CVSL Kameswari
III. The security/asset cover shall be arrived at after reduction of the liabilities having a first/prior charge, in case the convertible debt instruments are secured by a second or subsequent charge.

(2) The issuer shall redeem the convertible debt instruments in terms of the offer document.

Roll over of non convertible portion of partly convertible debt instruments.

21. (1) The non-convertible portion of partly convertible debt instruments issued by a listed issuer, the value of which exceeds fifty lakh rupees, may be rolled over without change in the interest rate, subject to compliance with the provisions of section 121 of the Companies Act, 1956 and the following conditions:

a) Seventy five per cent. Of the holders of the convertible debt instruments of the issuer have, through a resolution, approved the rollover through postal ballot;

b) The issuer has, along with the notice for passing the resolution, sent to all holders of the convertible debt instruments, an auditors’ certificate on the cash flow of the issuer and with comments on the liquidity position of the issuer;

c) The issuer has undertaken to redeem the non-convertible portion of the partly convertible debt instruments of all the holders of the convertible debt instruments who have not agreed to the resolution;

d) Credit rating has been obtained from at least one credit rating agency registered with the Board within a period of six months prior to the due date of redemption and has been communicated to the holders of the convertible debt instruments, before the roll over;

2) The creation of fresh security and execution of fresh trust deed shall not be mandatory if the existing trust deed or the security documents provide for continuance of the security until redemption of secured convertible debt instruments;

Provided that whether the issuer is required to create fresh security and to execute fresh trust deed or not shall be decided by the debenture trustee.

Conversion of optionally convertible debt instruments into equity share capital.

22. (1) An issuer shall not convert its optionally convertible debt instruments into equity shares unless the holders of such convertible debt instruments have sent their positive consent to the issuer and non-receipt of reply to any notice sent by the issuer for this purpose shall not be construed as consent for conversion of any convertible debt instruments.
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(2) Where the value of the convertible portion of any convertible debt instruments issued by a listed issuer exceeds fifty lakh rupees and the issuer has not determined the conversion price of such convertible debt instruments at the time of making the issue, the holders of such convertible debt instruments shall be given the option of not converting the convertible portion into equity shares:

Provided that where the upper limit on the price of such convertible debt instruments and justification thereon is determined and disclosed to the investors at the time of making the issue, it shall not be necessary to give such option to the holders of the convertible debt instruments for converting the convertible portion into equity share capital within the said upper limit.

(3) Where an option is to be given to the holders of the convertible debt instruments in terms of sub-regulation (2) and if one or more of such holders do not exercise the option to convert the instruments into equity share capital at a price determined in the general meeting of the shareholders, the issuer shall redeem that part of the instruments within one month from the last date by which option is to be exercised, at a price which shall not be less than its face value.

(4) The provision of sub-regulation (3) shall not apply if such redemption is in terms of the disclosures made in the offer document.

Issue of convertible debt instruments for financing

23. No issuer shall issue convertible debt instruments for financing, replenishment of funds or for providing loan to or for acquiring shares of any person who is part of the same group or who is under the same management:

Provided that an issuer may issue fully convertible debt instruments for these purposes if the period of conversion of such debt instruments is less than eighteen months from the date of issue of such debt instruments.

Explanation: For the purpose of this regulation:

(I) Two persons shall be deemed to be “part of the same group” if they belong to the group within the meaning of clause (ef) of section 2 of the Monopolies and Restrictive Trade Practices Act, 1969 (54 of 1969) or if they own “inter connected undertakings within the meaning of clause (g) of section 2 of the said Act;

(II) The expression “under the same management” shall have the same meaning as assigned to it in sub-section (1B) of section 370 of the Companies Act, 1956 (1 of 1956).
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Alteration of rights of holders of specified securities

24. No issuer shall alter the terms (including the terms of issue) of specified securities which may adversely affect the interests of the holders of that specified securities, except with the consent in writing of the holders of not less than three-fourths of the specified securities of that class or with the sanction of a special resolution passed at a meeting of the holders of the specified securities of that class.

CHAPTER III PROVISIONS AS TO PUBLIC ISSUE

PART I - ELIGIBILITY REQUIREMENTS Reference date

25. Unless otherwise provided in this Chapter, an issuer making a public issue shall satisfy the Conditions of this Chapter as on the date of filing draft offer document with the Board and also as on the date of registering the offer document with the Registrar of Companies.

Conditions for initial public offer.

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

   a) It has net tangible assets of at least three crore rupees in each of the preceding three full years (of twelve months each), of which not more than fifty per cent. Are held in monetary assets: Provided that if more than fifty per cent. of the net tangible assets are held in monetary assets, the issuer has made firm commitments to utilise such excess monetary assets in its business or project; 23[Provided further that the limit of fifty per cent. on monetary assets shall not be applicable in case the public offer is made entirely through an offer for sale.]

   b) 24[It has a track record of distributable profits in terms of section 205 of the Companies Act, 1956, on both stand-alone as well as consolidated basis for at least three out of the immediately preceding five years;] Provided that extraordinary items shall not be considered for calculating distributable profits; 25[Provided further that an issuer who had subsidiary/ subsidiaries for a period lesser Than five years, shall have net profits on a consolidated basis in at least one year for which consolidated accounts are prepared.]

   c) It has a net worth of at least one crore rupees in each of the preceding three full years (Of twelve months each);
d) The aggregate of the proposed issue and all previous issues made in the same financial year in terms of issue size does not exceed five times its pre-issue net worth as per the audited balance sheet of the preceding financial year;

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

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

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

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

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

or

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

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

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

(3) An issuer may make an initial public offer of convertible debt instruments without making a prior public issue of its equity shares and listing thereof.

(4) An issuer shall not make an allotment pursuant to a public issue if the number of prospective allottees is less than one thousand.

[(5) No issuer shall make an initial public offer if there are any outstanding convertible securities]
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Or any other right which would entitle any person with any option to receive equity shares:] provided that the provisions of this sub-regulation shall not apply to:

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

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

[(c) fully paid-up outstanding convertible securities which are required to be converted on or Before the date of filing of the red herring prospectus (in case of book-built issues) or the prospectus (in case of fixed price issues), as the case may be.]

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

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

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

a) In case of an offer for sale of specified securities of a government company or statutory authority or corporation or any special purpose vehicle set up and controlled by any one or more of them, which is engaged in infrastructure sector;

b) If the specified securities offered for sale were acquired pursuant to any scheme approved by a High Court under sections 391-394 of the Companies Act, 1956, in lieu of business and invested capital which had been in existence for a period of more than one year prior to such approval.

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

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

II. "Project" means the object for which monies are proposed to be raised to cover the objects of the issue;

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

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

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

      I. The accounts and the disclosures made are in accordance with the provisions of Schedule VI of the Companies Act, 1956;

      II. The accounting standards of the Institute of Chartered Accountants of India have been followed;

      III. The financial statements present a true and fair view of the firm's accounts;

      IV. In case of an issuer formed out of a division of an existing company, the track record of distributable profits of the division spun-off shall be considered only if the requirements regarding financial statements as provided for partnership firms in Explanation III are complied with;

      V. "Bid-ask spread" means the difference between quotations for sale and purchase;

      VI. The term "infrastructure sector" includes the facilities or services as specified in Schedule X.

Conditions for further public offer

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

PART II - PRICING IN PUBLIC ISSUE

Pricing

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

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

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

Differential pricing

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

a) Retail individual investors or retail individual shareholders 28[or employees 29[***] entitled for reservation made under regulation 42 making an application for specified securities of value not more than 30[two lakhs] rupees,] may be offered specified securities at a price lower than the price at which net offer is made to other categories of applicants: Provided that such difference shall not be more than ten per cent. Of the price at which specified securities are offered to other categories of applicants;

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

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

[(d) In case the issuer opts for the alternate method of book building in terms of Part D of Schedule XI, the issuer may offer specified securities to its employees at a price lower than the floor price: Provided that the difference between the floor price and the price at which specified Securities are offered to employees shall not be more than ten per cent. Of the floor price.]
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Price and price band

30. (1) The issuer may mention a price or price band in the draft prospectus (in case of a fixed price issue) and floor price or price band in the red herring prospectus (in case of a book built issue) and determine the price at a later date before registering the prospectus with the Registrar of Companies: Provided that the prospectus registered with the Registrar of Companies shall contain only one price or the specific coupon rate, as the case may be.

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

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

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

(5) The floor price or the final price shall not be less than the face value of the specified securities. Explanation: For the purposes of sub-regulation (4), the "cap on the price band" includes cap on the coupon rate in case of convertible debt instruments.

Face value of equity shares

31. (1) Subject to the provisions of the Companies Act, 1956, the Act and these regulations, an issuer making an initial public offer may determine the face value of the equity shares in the following manner:

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

b) If the issue price per equity share is less than five hundred rupees, the face value of the equity shares shall be ten rupees per equity share: Provided that nothing contained in this sub-regulation shall apply to initial public offer made by any government company, statutory authority or corporation or any special purpose vehicle set up by any of them, which is engaged in infrastructure sector.

Researcher: CVSL Kameswari
(2) The disclosure about the face value of equity shares (including the statement about the issue price being "X" times of the face value) shall be made in the advertisements, offer documents and application forms in identical font size as that of issue price or price band.

Explanation: For the purposes of this regulation, the term "infrastructure sector" includes the facilities or services as specified in Schedule X.

PART III - PROMOTERS' CONTRIBUTION

Minimum promoter's contribution

32. (1) The promoters of the issuer shall contribute in the public issue as follows:

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

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

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

(2) In case of a public issue or composite issue of convertible securities, minimum promoters' Contribution shall be as follows:

a) The promoters shall contribute twenty per cent. As stipulated in clauses (a), (b) or (c) of sub-regulation (1), as the case may be, either by way of equity shares or by way of subscription to the convertible securities: Provided that if the price of the equity shares allotted pursuant to conversion is not pre- determined and not disclosed in the offer document, the promoters shall contribute only by way of subscription to the convertible securities being issued in the public issue and shall undertake in writing to subscribe to the equity shares pursuant to conversion of such securities.

b) In case of any issue of convertible securities which are convertible or exchangeable on different dates and if the promoters' contribution is by way of equity shares (conversion price being pre-determined), such contribution shall not be at a price lower than the weighted average price of the equity share capital arising out of conversion of such securities.
c) Subject to the provisions of clause (a) and (b) above, in case of an initial public offer of convertible debt instruments without a prior public issue of equity shares, the promoters shall bring in a contribution of at least twenty per cent. Of the project cost in the form of equity shares, subject to contributing at least twenty per cent. Of the issue size from their own funds in the form of equity shares: Provided that if the project is to be implemented in stages, the promoters' contribution shall be with respect to total equity participation till the respective stage vis-à-vis the debt raised or proposed to be raised through the public issue.

(3) In case of a further public offer or composite issue where the promoters contribute more than the stipulated minimum promoters' contribution, the allotment with respect to excess contribution shall be made at a price determined in terms of the provisions of regulation 76 or the issue price, whichever is higher.

(4) The promoters shall satisfy the requirements of this regulation at least one day prior to the date of opening of the issue and the amount of promoters' contribution shall be kept in an escrow account with a scheduled commercial bank and shall be released to the issuer along with the release of the issue proceeds:

Provided that where the promoters’ contribution has already been brought in and utilised, the issuer shall give the cash flow statement disclosing the use of such funds in the offer document; Provided further that where the minimum promoters’ contribution is more than one hundred crore rupees, the promoters shall bring in at least one hundred crore rupees before the date of opening of the issue and the remaining amount may be brought on pro-rata basis before the calls are made to public.

Explanation: For the purpose of this regulation:

I. Promoters' contribution shall be computed on the basis of the post-issue expanded capital:
   a) Assuming full proposed conversion of convertible securities into equity shares;
   b) Assuming exercise of all vested options, where any employee stock options are outstanding at the time of initial public offer in terms of proviso (b) to sub-regulation (5) of regulation 26.

II. For computation of “weighted average price”:
   a) “Weights” means the number of equity shares arising out of conversion of such specified securities into equity shares at various stages;
b) "price" means the price of equity shares on conversion arrived at after taking into account predetermined conversion price at various stages.

Securities ineligible for minimum promoters' contribution

33. (1) For the computation of minimum promoters' contribution, the following specified securities shall not be eligible:

a) Specified securities acquired during the preceding three years, if they are:

I. Acquired for consideration other than cash and revaluation of assets or capitalisation of intangible assets is involved in such transaction; or

II. Resulting from a bonus issue by utilisation of revaluation reserves or unrealised profits of the issuer or from bonus issue against equity shares which are ineligible for minimum promoters' contribution;

b) Specified securities acquired by promoters during the preceding one year at a price lower than the price at which specified securities are being offered to public in the initial public offer: Provided that nothing contained in this clause shall apply:

I. If promoters pay to the issuer, the difference between the price at which specified securities are offered in the initial public offer and the price at which the specified securities had been acquired;

II. If such specified securities are acquired in terms of the scheme under sections 391-394 of the Companies Act, 1956, as approved by a High Court, by promoters in lieu of business and invested capital that had been in existence for a period of more than one year prior to such approval;

III. To an initial public offer by a government company, statutory authority or corporation or any special purpose vehicle set up by any of them, which is engaged in infrastructure sector;

c) Specified securities allotted to promoters during the preceding one year at a price less than the issue price, against funds brought in by them during that period, in case of an issuer formed by conversion of one or more partnership firms, where the partners of the erstwhile partnership firms are the promoters of the issuer and there is no change in the management: Provided that specified securities, allotted to promoters against capital existing in such firms for a period of more than one year on a continuous basis, shall be eligible;

d) Specified securities pledged with any creditor.
(2) Specified securities referred to in clauses (a) and (c) of sub-regulation (1) shall be eligible for the computation of promoters' contribution, if such securities are acquired pursuant to a scheme which has been approved under sections 391-394 of the Companies Act, 1956.

Explanation: For the purposes of clause (b) of sub-regulation (1), the term "infrastructure sector" includes the facilities or services as specified in Schedule X. Requirement of minimum promoters' contribution not applicable in certain cases.

34. The requirements of minimum promoters' contribution shall not apply in case of:

a) An issuer which does not have any identifiable promoter;

b) A further public offer, where the equity shares [of the issuer] [***] are not infrequently traded in a recognised stock exchange for a period of at least three years and the issuer has a track record of dividend payment for at least immediately preceding three years: Provided that where promoters propose to subscribe to the specified securities offered to the extent greater than higher of the two options available in clause (b) of sub-regulation (1) of regulation 32, the subscription in excess of such percentage shall be made at a price determined in terms of the provisions of regulation 76 or the issue price, whichever is higher.

c) Rights issues.

Explanation: For the purpose of clause (b), the words "infrequently traded" have the same meaning as assigned to them in Explanation to sub-regulation (5) of regulation 20 of the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 1997 and the reference date for the purpose of computing the annualised trading turnover referred to in the said Explanation shall be the date of filing the draft offer document with the Board and in case of a fast track issue, the date of filing the offer document with the Registrar of Companies before opening of the issue.
PART IV - RESTRICTION ON TRANSFERABILITY (LOCK-IN) OF PROMOTERS' CONTRIBUTION, ETC

Date of commencement of lock in and inscription of non-transferability.

35. (1) Save as otherwise provided in this Chapter, specified securities held by promoters and persons other than promoters shall not be transferable (hereinafter referred to as "lock-in") from the date of allotment of the specified securities in the proposed public issue for the period stipulated in this Chapter.

(2) The certificate of specified securities which are subject to lock-in shall contain the inscription “non transferable” and the lock-in period and in case such specified securities are dematerialised, the issuer shall ensure that lock-in is recorded by the depository.

(3) Where the specified securities which are subject to lock-in are partly paid-up and the amount called-up on such specified securities is less than the amount called-up on the specified securities issued to the public, the "lock-in" shall end only on the expiry of three years after such specified securities have become pari-passu with the specified securities issued to the public.

Lock-in of specified securities held by promoters

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

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

b) Promoters' holding in excess of minimum promoters' contribution shall be locked-in for a period of one year: Provided that excess promoters' contribution as provided in proviso to clause (b) of regulation 34 shall not be subject to lock-in.

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

Lock-in of specified securities held by persons other than promoters

Researcher: CVSL Kameswari
37. In case of an initial public offer, the entire pre-issue capital held by persons other than promoters shall be locked-in for a period of one year: Provided that nothing contained in this regulation shall apply to:

   a) Equity shares allotted to employees under an employee stock option or employee stock purchase scheme of the issuer prior to the initial public offer, if the issuer has made full disclosures with respect to such options or scheme in accordance with Part A of Schedule VIII;

   b) Equity shares held by a venture capital fund or a foreign venture capital investor for a period of at least one year prior to the date of filing the draft prospectus with the Board:

Explanation: For the purpose of clause (b), in case such equity shares have resulted pursuant to conversion of fully paid-up compulsorily convertible securities, the holding period of such convertible securities as well as that of resultant equity shares together shall be considered for the purpose of calculation of one year period and convertible securities shall be deemed to be fully paid-up, if the entire consideration payable thereon has been paid and no further consideration is payable at the time of their conversion.

Lock-in of specified securities lent to stabilising agent under green shoe option

38. The lock-in provisions of this Chapter shall not apply with respect to the specified securities lent to stabilising agent for the purpose of green shoe option, during the period starting from the date of lending of such specified securities and ending on the date on which they are returned to the lender in terms of sub-regulation (5) or (6) of regulation 45:

Provided that the specified securities shall be locked-in for the remaining period from the date on which they are returned to the lender.

Pledge of locked-in specified securities

39. Specified securities held by promoters and locked-in may be pledged with any scheduled commercial bank or public financial institution as collateral security for loan granted by such bank or institution, subject to the following:

   a) If the specified securities are locked-in in terms of clause (a) of regulation 36, the loan has been granted by such bank or institution for the purpose of financing one or more of the objects of the issue and pledge of specified securities is one of the terms of sanction of the loan;

   b) If the specified securities are locked-in in terms of clause (b) of regulation 36 and the pledge of specified securities is one of the terms of sanction of the loan.
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Transferability of locked-in specified securities

40. Subject to the provisions of Securities and Exchange Board of India (Substantial Acquisition of shares and Takeovers) Regulations, 1997, the specified securities held by promoters and locked-in as per regulation 36 may be transferred to another promoter or any person of the promoter group or a new promoter or a person in control of the issuer and the specified securities held by persons other than promoters and locked-in as per regulation 37 may be transferred to any other person holding the specified securities which are locked-in along with the securities proposed to be transferred:

Provided that lock-in on such specified securities shall continue for the remaining period with the transferee and such transferee shall not be eligible to transfer them till the lock-in period stipulated in these regulations has expired.

PART V - MINIMUM OFFER TO PUBLIC, RESERVATIONS, ETC

Minimum offer to public

41. (1) Subject to the provisions of sub-clause (b) of clause (2) of rule 19 of Securities Contracts (Regulations) Rules, 1957, the net offer to public:

a) In case of an initial public offer, shall be at least ten per cent. Of twenty five per cent. Of the post-issue capital, as the case may be; and

b) In case of a further public offer, shall be at least ten per cent. Of twenty five per cent. Of the issue size, as the case may be.

(2) Nothing contained in sub-regulation (1) shall apply if the issuer is:

a) A government company or statutory authority or corporation or any special purpose vehicle set up and controlled by any one or more of them, which is engaged in infrastructure sector;

b) An infrastructure company fulfilling the following conditions:

I. Its project has been appraised by one or more public financial institutions;

II. Not less than fifty per cent. of the project cost is financed by one or more such institutions, jointly or severally, by way of loan or subscription to equity shares or a combination of both, irrespective of whether they appraise the project or not.
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Explanation: For the purpose of this regulation:

I. The term “infrastructure company” means, an enterprise wholly engaged in the business of (i) developing or (ii) operating and maintaining or (iii) developing, operating and maintaining any infrastructure facility;

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

Reservation on competitive basis

42. (1) In case of an issue made through the book building process, the issuer may make reservation on competitive basis out of the issue size excluding promoters’ contribution and net offer to public in favour of the following categories of persons:

a) ([employees; and in case of a new issuer, persons who are in the permanent and full time Employment of the promoting companies excluding the promoters and an immediate relative of the promoter of such companies;]

b) Shareholders (other than promoters) of:

(i) Listed promoting companies, in case of a new issuer; and

(ii) listed group companies, in case of an existing issuer: Provided that if the promoting companies are designated financial institutions or state and central financial institutions, the shareholders of such promoting companies shall not be eligible for the reservation on competitive basis;

c) Persons who, as on the date of filing the draft offer document with the Board, are associated with the issuer as depositors, bondholders or subscribers to services of the issuer making an initial public offer:

Provided that the issuer shall not make the reservation to the issue management team, syndicate members, their promoters, directors and employees and for the group or associate companies of the issue management team and syndicate members and their promoters, directors and employees;

2) In case of an issue made other than through the book building process, the issuer may make reservation on competitive basis out of the issue size excluding promoters’ contribution and net offer to public in favour of the following categories of persons:

a) [employees; and in case of a new issuer, persons who are in the permanent and full time
b) Employment of the promoting companies excluding the promoters and an immediate relative of the promoter of such companies;

c) Shareholders (other than promoters) of:

I. Listed promoting companies, in the case of a new issuer; and

II. Listed group companies, in the case of an existing issuer:

Provided that if the promoting companies are designated financial institutions or state and central financial institutions, the shareholders of such promoting companies shall not be eligible for the reservation on competitive basis.

(3) In case of a further public offer (not being a composite issue), the issuer may make reservation on competitive basis out of the issue size excluding promoters' contribution and net offer to public in favour of retail individual shareholders of the issuer.

(4) The reservation on competitive basis shall be subject to following conditions:

a) The aggregate of reservations for employees shall not exceed 36[five per cent. of the post issue capital of the issuer];

b) Reservation for shareholders shall not exceed ten per cent. Of the issue size;

c) Reservation for persons who as on the date of filing the draft offer document with the Board, have business association as depositors, bondholders and subscribers to services with the issuer making an initial public offer shall not exceed five per cent. Of the issue size;

d) No further application for subscription in the net offer to public category shall be entertained from any person (except an employee and retail individual shareholder) in favour of whom reservation on competitive basis is made;

e) Any unsubscribed portion in any reserved category may be added to any other reserved category and the unsubscribed portion, if any, after such inter-se adjustments among the reserved categories shall be added to the net offer to the public category;

f) In case of under-subscription in the net offer to the public category, spill-over to the extent of under-subscription shall be permitted from the reserved category to the net public offer category;

g) 37[value of allotment to any employee in pursuance of reservation made under sub-Regulations (1) or (2), as the case may be, shall not exceed 38[two lakhs] rupees.]

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(5) In the case of reserved categories, a single applicant in the reserved category may make an application for a number of specified securities which exceeds the reservation.

**Explanation:** For the purposes of this regulation:

I. The term "reservation on competitive basis" means reservation wherein specified securities are allotted in proportion of the number of specified securities applied for in respect of a particular reserved category to the number of specified securities reserved for that category;

II. The term "new issuer" means an issuer which has not completed twelve months of commercial operation and its audited operative results are not available.

**Allocation in net offer to public**

43. (1) No person shall make an application in the net offer to public category for that number of specified securities which exceeds the number of specified securities offered to public.

(2) In an issue made through the book building process, the allocation in the net offer to public category shall be made as follows:

a) Not less than thirty five per cent. To retail individual investors;

b) Not less than fifteen per cent. To non-institutional investors;

c) Not more than fifty per cent. To qualified institutional buyers, five per cent. Of which shall be allocated to mutual funds:

Provided that in case of an issue made in terms of sub-clause (i) of clause (a) of sub-regulation (2) of regulation 26, at least fifty per cent. Of the net offer to public shall be allotted to qualified institutional buyers:

[*[*]] Provided further that in addition to five per cent. Allocation available in terms of clause (c), mutual funds shall be eligible for allocation under the balance available for qualified institutional buyers.

(3) In an issue made through the book building process, the issuer may allocate up to thirty per cent. Of the portion available for allocation to qualified institutional buyers to an anchor investor in accordance with the conditions specified in this regard in Schedule XI.

(4) In an issue made other than through the book building process, allocation in the net offer to public category shall be made as follows:

a) Minimum fifty per cent. To retail individual investors; and
b) Remaining to:
   • Individual applicants other than retail individual investors; and
   • Other investors including corporate bodies or institutions, irrespective of the number of specified securities applied for;

c) The unsubscribed portion in either of the categories specified in clauses (a) or (b) may be allocated to applicants in the other category.

Explanation: For the purpose of sub-regulation (4), if the retail individual investor category is entitled to more than fifty per cent. On proportionate basis, the retail individual investors shall be allocated that higher percentage.

Safety-net arrangement

44. An issuer may provide for a safety-net arrangement for the specified securities offered in any public issue in consultation with the merchant banker after ascertaining the financial capacity of the person offering the safety-net arrangement, subject to disclosures specified in this regard in Part A of Schedule VIII:

Provided that any such arrangement shall provide for an offer to purchase up to a maximum of one thousand specified securities per original resident retail individual allottee at the issue price within a period of six months from the last date of despatch of security certificates or credit of demat account.

Explanation: For the purpose of this regulation, the term “safety net arrangement” means an arrangement provided by the issuer under which a person offers to purchase specified securities from the original resident retail individual allottees at the issue price.

Price stabilisation through green shoe option

45. (1) An issuer making a public issue of specified securities may provide green shoe option for stabilising the post listing price of its specified securities, subject to the following:

   a) The issuer has been authorized, by a resolution passed in the general meeting of shareholders approving the public issue, to allot specified securities to the stabilising agent, if required, on the expiry of the stabilisation period;

   b) The issuer has appointed a merchant banker or book runner, as the case may be, from amongst the merchant bankers appointed by the issuer as a stabilising agent, who shall be responsible for the price stabilisation process;
c) Prior to filing the draft offer document with the Board, the issuer and the stabilising agent have entered into an agreement, stating all the terms and conditions relating to the green shoe option including fees charged and expenses to be incurred by the stabilising agent for discharging his responsibilities;

d) Prior to filing the offer document with the Board, the stabilising agent has entered into an agreement with the promoters or pre-issue shareholders or both for borrowing specified securities from them in accordance with clause (g) of this sub-regulation, specifying therein the maximum number of specified securities that may be borrowed for the purpose of allotment or allocation of specified securities in excess of the issue size (hereinafter referred to as the "over-allotment"), which shall not be in excess of fifteen per cent. Of the issue size;

e) Subject to clause (d), the lead merchant banker or lead book runner, in consultation with the stabilising agent, shall determine the amount of specified securities to be over-allotted in the public issue;

f) The draft and final offer documents shall contain all material disclosures about the green shoe option specified in this regard in Part A of Schedule VIII;

g) In case of an initial public offer pre-issue shareholders and promoters and in case of a further public offer pre-issue shareholders holding more than five per cent. Specified securities and promoters may lend specified securities to the extent of the proposed over-allotment;

h) The specified securities borrowed shall be in dematerialised form and allocation of these securities shall be made pro-rata to all successful applicants.

(2) For the purpose of stabilisation of post-listing price of the specified securities, the stabilising agent shall determine the relevant aspects including the timing of buying such securities, quantity to be bought and the price at which such securities are to be bought from the market.

(3) The stabilisation process shall be available for a period not exceeding thirty days from the date on which trading permission is given by the recognised stock exchanges in respect of the specified securities allotted in the public issue.

(4) The stabilising agent shall open a special account, distinct from the issue account, with a bank for crediting the monies received from the applicants against the over-allotment and a special account with a depository participant for crediting specified securities to be bought from the market during the stabilisation period out of the monies credited in the special bank account.
5) The specified securities bought from the market and credited in the special account with the depository participant shall be returned to the promoters or pre-issue shareholders immediately, in any case not later than two working days after the end of the stabilization period.

(6) On expiry of the stabilisation period, if the stabilising agent has not been able to buy specified securities from the market to the extent of such securities over-allotted, the issuer shall allot specified securities at issue price in dematerialised form to the extent of the shortfall to the special account with the depository participant, within five days of the closure of the stabilisation period and such specified securities shall be returned to the promoters or pre-issue shareholders by the stabilising agent in lieu of the specified securities borrowed from them and the account with the depository participant shall be closed thereafter.

(7) The issuer shall make a listing application in respect of the further specified securities allotted under sub-regulation (6), to all the recognised stock exchanges where the specified securities allotted in the public issue are listed and the provisions of Chapter VII shall not be applicable to such allotment.

(8) The stabilising agent shall remit the monies with respect to the specified securities allotted under sub-regulation (6) to the issuer from the special bank account.

(9) Any monies left in the special bank account after remittance of monies to the issuer under sub- regulation (8) and deduction of expenses incurred by the stabilising agent for the stabilisation process shall be transferred to the Investor Protection and Education Fund established by the Board and the special bank account shall be closed soon thereafter.

(10) The stabilising agent shall submit a report to the stock exchange on a daily basis during the stabilisation period and a final report to the Board in the format specified in Schedule XII.

(11) The stabilising agent shall maintain a register for a period of at least three years from the date of the end of the stabilisation period and such register shall contain the following particulars:

- The names of the promoters or pre-issue shareholders from whom the specified securities were borrowed and the number of specified securities borrowed from each of them;
- The price, date and time in respect of each transaction effected in the course of the stabilisation process;
- The details of allotment made by the issuer on expiry of the stabilisation process.
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Period of subscription

46. (1) [Except as otherwise provided in these regulations] a public issue shall be kept open for at least three working days but not more than ten working days including the days for which the issue is kept open in case of revision in price band.

(2) In case the price band in a public issue made through the book building process is revised, the bidding (issue) period disclosed in the red herring prospectus shall be extended for a minimum period of three working days:

Provided that the total bidding period shall not exceed ten working days.

Pre-issue advertisement for public issue.

47. (1) Subject to the provisions of section 66 of the Companies Act, 1956, the issuer shall, after registering the red herring prospectus (in case of a book built issue) or prospectus (in case of fixed price issue) with the Registrar of Companies, make a pre-issue advertisement in one English national daily newspaper with wide circulation, Hindi national daily newspaper with wide circulation and one regional language newspaper with wide circulation at the place where the registered office of the issuer is situated.

(2) The pre-issue advertisement shall be in the format and shall contain the disclosures specified in Part A of Schedule XIII.

Issue opening and issue closing advertisement for public issue.

48. An issuer may issue advertisements for issue opening and issue closing advertisements, which shall be in the formats specified in Parts B and C of Schedule XIII.

Minimum application value

49. (1) the issuer shall stipulate in the offer document, the minimum application size in terms of number of specified securities which shall fall within the range of minimum application value of five thousand rupees to seven thousand rupees.

(2) The issuer shall invite applications in multiples of the minimum application value, an illustration whereof is given in Schedule XIV.

(3) The minimum sum payable on application shall not be less than twenty five per cent. Of the issue price:

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Provided that in case of an offer for sale, the issue price payable for each specified security shall be brought in at the time of application.

Explanation: For the purpose of this regulation, "minimum application value" shall be with reference to the issue price of the specified securities and not with reference to the amount payable on application.

Allotment procedure and basis of allotment.

50. (1) The allotment of specified securities to applicants other than anchor investors shall be on proportionate basis within the specified investor categories and the number of securities allotted shall be rounded off to the nearest integer, subject to minimum allotment being equal to the minimum application size as determined and disclosed by the issuer:

(2) The executive director or managing director of the designated stock exchange along with the post issue lead merchant bankers and registrars to the issue shall ensure that the basis of allotment is finalised in a fair and proper manner in accordance with the allotment procedure as specified in Schedule XV.

Utilisation of subscription money

51. The post-issue lead merchant banker shall ensure that moneys received in respect of the issue are released to the issuer in compliance with the provisions of section 73 of the Companies Act, 1956.
CHAPTER IV RIGHTS ISSUE

Record Date

52. (1) A listed issuer making a rights issue shall announce a record date for the purpose of determining the shareholders eligible to apply for specified securities in the proposed rights issue.

(2) The issuer shall not withdraw rights issue after announcement of the record date.

(3) If the issuer withdraws the rights issue after announcing the record date, it shall not make an application for listing of any of its specified securities on any recognised stock exchange for a period of twelve months from the record date announced under sub-regulation (1):

Provided that the issuer may seek listing of its equity shares allotted pursuant to conversion or exchange of convertible securities issued prior to the announcement of the record date, on the recognised stock exchange where its securities are listed.

Restriction on rights issue

53. (1) No issuer shall make a rights issue of equity shares 43[**] unless it has made reservation of equity shares of the same class in favour of the holders of 44[**] outstanding 45[compulsorily] convertible debt instruments 46[, if any,] in proportion to the convertible part thereof.

(2) The equity shares 47[so] reserved for the holders of fully or partially 48[compulsorily]

Convertible debt instruments shall be issued at the time of conversion of such convertible debt instruments on the same terms 49[at] which the equity shares offered in the rights issue were issued.

Letter of offer, abridged letter of offer, pricing and period of subscription.

54.(1) The abridged letter of offer, along with application form, shall be dispatched through registered post or speed post to all the existing shareholders at least three days before the date of opening of the issue:

Provided that the letter of offer shall be given by the issuer or lead merchant banker to any existing shareholder who has made a request in this regard.

(2) The shareholders who have not received the application form may apply in writing on a plain paper, along with the requisite application money.
(3) The shareholders making application otherwise than on the application form shall not renounce their rights and shall not utilise the application form for any purpose including renunciation even if it is received subsequently.

(4) Where any shareholder makes an application on application form as well as on plain paper, the application is liable to be rejected.

5) The issue price shall be decided before determining the record date which shall be determined in consultation with the designated stock exchange.

(6) A rights issue shall be open for subscription for a minimum period of fifteen days and for a maximum period of thirty days.

[(7) the issuer shall give only one payment option out of the following to all the investors—

(a) Part payment on application with balance money to be paid in calls; or

(b) Full payment on application:

Provided that where the issuer has given the part payment option to investors, such issuer shall obtain the necessary regulatory approvals to facilitate the same.]

Pre-Issue Advertisement for rights issue

55. (1) The issuer shall issue an advertisement for rights issue disclosing the following:

a) The date of completion of despatch of abridged letter of offer and the application form;

b) The centres other than registered office of the issuer where the shareholders or the persons entitled to receive the rights entitlements may obtain duplicate copies of the application forms in case they do not receive the application form within a reasonable time after opening of the rights issue;

c) A statement that if the shareholders entitled to receive the rights entitlements have neither received the original application forms nor they are in a position to obtain the duplicate forms, they may make application in writing on a plain paper to subscribe to the rights issue;

d) A format to enable the shareholders entitled to apply against their rights entitlements, to make the application on a plain paper specifying therein necessary particulars such as name, address, ratio of rights issue, issue price, number of equity shares held, ledger folio numbers, depository participant ID, client ID, number of equity shares entitled and

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applied for, additional shares if any, amount to be paid along with application, and particulars of cheque, etc. to be drawn in favour of the issuer’s account;

e) A statement that the applications can be directly sent by the shareholders entitled to apply against rights entitlements through registered post together with the application moneys to the issuer's designated official at the address given in the advertisement;

f) A statement to the effect that if the shareholder makes an application on plain paper and also on application form both his applications shall be liable to be rejected at the option of the issuer.

(2) The advertisement shall be made in at least one English national daily newspaper with wide circulation, one Hindi national daily newspaper with wide circulation and one regional language daily newspaper with wide circulation at the place where registered office of the issuer is situated, at least three days before the date of opening of the issue.

51[Reservation for employees along with rights issue.

55A. Subject to other applicable provision of these regulations the issuer may make reservation for 52[***] employees along with rights issue subject to the condition that value of allotment to any employee shall not exceed [two lakhs] rupees.]

Utilisation of funds raised in rights issue

56. The issuer shall utilise funds collected in rights issues after the finalisation of the basis of allotment.
CHAPTER V - MANNER OF DISCLOSURES IN THE OFFER DOCUMENTS

Manner of disclosures in the offer document

57. (1) the offer document shall contain all material disclosures which are true and adequate so as to enable the applicants to take an informed investment decision.

(2) Without prejudice to the generality of sub-regulation (1):

(a) The red-herring prospectus, shelf prospectus and prospectus shall contain:

   - The disclosures specified in Schedule II of the Companies Act, 1956; and
   - The disclosures specified in Part a of Schedule VIII, subject to the provisions of Parts B and C thereof.

(b) The letter of offer shall contain disclosures as specified in Part E of Schedule VIII.

Abridged prospectus, abridged letter of offer and ASBA

58. (1) The abridged prospectus shall contain the disclosures of the memorandum prescribed under sub-section (3) of section 56 of the Companies Act, 1956 and additional disclosures as specified in Part D of Schedule VIII.

(2) The abridged letter of offer shall contain the disclosures as specified in Part F of Schedule VIII.

(3) The abridged prospectus and abridged letter of offer shall not contain any matter extraneous to the contents of the offer document.

(4) Every application form including ASBA form distributed by the issuer or any other person in relation to an issue shall be accompanied by a copy of the abridged prospectus or abridged letter of offer, as the case may be.
SECONDARY MARKET / STOCK MARKET / STOCK EXCHANGE

One of the criteria in investment management which is considered as very important next to risk assessment is the liquidity. After the investors get the shares allotted through the primary market they need some platform or market place to provide liquidity for their investment. Thus, secondary market offers liquidity to investment made in the primary market. Both, primary and secondary markets co-exist, i.e. to say one depends on the other for its survival and growth.

There are two broad segments of the stock markets (i) The organised stock exchanges and (ii) The Over-the-Counter (OTC) market. The primary middlemen in the stock market are brokers and dealers.

The distinction between them is, the broker acts as an agent, whereas the dealer acts as a principal in the transaction. Stock markets are said to reflect the overall health of the country's economy. On the other hand, major economic indicators determine stock market movements to a large extent.

From a thorough analysis of the various economic Indicators and its implications on the stock markets, it is known that stock market movements are largely influenced by broad money supply, inflation, credit/deposit ratio and fiscal deficit apart from political stability. Besides, fundamental factors like corporate performance, industrial growth, etc. always exert a certain amount of influence on the stock markets.

Because the stock market involves the trading of securities initially sold in the primary market, it is providing liquidity to the individuals who acquired these securities. The trends in stock market will have impact on the primary market. The secondary market in India comprises of 23 Stock Exchanges and more than 10000 listed companies out of which BSE has about 4888 and NSE has 1225 companies listed with them as on 29th February 2008.

A large volume of transactions on the secondary markets are transacted through BSE and NSE. Presently, the BSE & NSE put together account for more than 99% of the total turnover as compared to less than 1% by the other Stock Exchanges.

Reasons for Transactions on Secondary Market

There are two main reasons why individuals transact in the secondary market: Information Motivated Reasons: Information motivated investors believe that they have superior information about a particular security than other market participants. This information leads them to believe that the security is not being correctly priced by the market.

If the information is good, this suggests that the security is currently under-priced, and investors with access to such information will want to buy the security. On the other hand, if the
information is bad, the security will be currently overpriced, and such investors will want to sell their holdings of the security.

Liquidity Motivated Reasons: Liquidity motivated investors, on the other hand, transact in the secondary market because they are currently in a position of either excess or insufficient liquidity. Investors with surplus cash holdings (e.g., as a result of an inheritance or adequate savings of their income) will buy securities, where as investors with insufficient cash (e.g., to purchase a car or any other assets) will sell their securities.

The Securities which are traded in the secondary market may be classified as follows.

1. On the basis of issuer, Securities may be classified as
   - Industrial securities,
   - Government securities
   - Financial intermediary's securities.

Industrial securities issued by industrial and common undertakings in the private and public sector whereas government securities include securities issued by State governments, meniscopolities and public utilities. Government securities are generally considered risk-free, low return securities compared to the Industrial securities.

Besides these two classes of issues, the Financial Intermediaries are emerging as the third important group. The securities issued by Financial Institutions and Banks would fall, in terms of risk-return features, somewhere in between the industrial securities and government securities.

On the basis of maturity, securities may be classified into short term and long term or Money Market and Capital Market securities. Treasury bills, commercial bills, commercial papers, certificate of deposits are short-term or money market securities. Equities, Performance shares, Debentures and Bonds are long term or capital market securities.

On the basis of settlement of deals, securities may be classified into Forward securities and cash securities. Forward securities are those in which the settlement date can be shifted from one settlement date to other by paying the bald charges. Cash securities are those for which settlement dates cannot be shifted. The Forward securities are known by different names viz. specified shares or group a shares or Forward section. Cash securities are also known as Non-specie-feed shares or group B shares or cash section.
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Stock Market in India

From scattered and small beginnings in the 19th Century, India's stock market has risen to great heights. In 1990, we had 19 stock exchanges in the country. There were around 6,000 listed companies and the invested population stood around 15 million.

You might be interested in knowing more about the growth of stock market in India. What functions does it perform? What is the form of organization of stock exchange in India? How are they administered? What is the trading system followed on these exchanges? We shall discuss these and other questions in the following sections.

Role and Functions of Stock Exchanges

The history of stock exchanges shows that the development of joint stock enterprise would never have reached its present stage but for the facilities which the stock exchanges provide for dealing with the securities. Stock exchanges have a very important function to fulfill in the country's economy.

The stock exchange is really an essential pillar of the private sector corporate economy. It discharges essential functions in the process of capital formation and in raising resources for the corporate sector.

First the stock exchange provides a market place for purchase and sale of securities viz., shares, bonds, debentures etc. It, therefore, ensures the free transferability of securities which is the essential basis for the stock enterprise system. The private sector economy cannot function without the assurance provided by the exchange to the owners of shares and bonds that they can be sold in the market at any time. At the same time, those who invest their surplus funds in securities for long-term capital appreciation or for speculative purpose can also buy scripts of their choice in the market.

Secondly, the stock exchange provides the linkage between the savings in the household sector and investment in corporate economy. It mobilizes savings, and channelizes them in the form of securities into those enterprises which are favoured by the investors on the basis of such criteria as future growth prospects, good returns and appreciation of capital.

Thirdly, by providing a market quotation of the prices of shares and bonds - a sort of collective judgement simultaneously reached by many buyers and sellers in the market-the stock exchange serves the role of barometer, not only of the state of health of individual companies, but also of the nation's economy. The changes in share prices are brought about by a complex set of factors, all operating in the market simultaneously. Share values as a whole are subject to secular trends set by the economic programme of the nation, and governed by factors

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like general economic situation, financial and monetary policies, tax changes, polity-cal environment, international - economic and financial development, etc.

Membership, organization and Management

Nature of the century-old traditional stock exchanges is a highly organized and smoothly functioning network in the world. The membership of stock exchanges initially comprised of individuals and partnership firms. Later on the corporate entities and financial institutions were also allowed to become members. A number of financial institutions are now members of Indian Stock Exchanges. Over the years, stock exchanges have been initiated in various forms. For example, while the Ahmadabad Stock Exchange and M.P. (Indore) Stock Exchange were started as Non-profit making association of persons, the Calcutta Stock Exchange, Delhi Stock Exchange, U.P. Stock Exchange, Cochin Stock Exchange, Gauhati Stock Exchange, Bangalore Stock Exchange, Jaipur Stock Exchange and (Mangalore) Stock Exchange were established as public limited companies. Quite a few others have been started as Company limited by guarantee.

The entrance fee is different for different stock exchanges. Membership deposit and annual fees also varies from exchange to exchange. The entrance fee is different for different members among various exchanges based on their status like individual or corporate. The internal governance of exchange rests in a governing board comprising members of the board and Exec-tie Director.

The Members of the governing boards include brokers and SEBI Nominees called Public Representatives. The Chairman is expected to ensure the position of Executive Director can't be expected to be very strong because if he really tries to be may bring him into conflict with influential broker-members who may also be on the exchange's board which determines Executive Director's terms and conditions of service and his re-appointment on this term.

It is not human nature to displease one's appointing authorities and it may be too much Executive Director's to be strict under the present scheme of things. Subject to the previous approval of the law, governing bodies of stock exchanges have wide powers to make bye-laws.

Governing bodies furnish, censure and also expel any member, any remise, and authorized clerk and employee. It has to adjudicate disputes. Above all, it has the power to make, amend, suspend and enforce rules, bye-regulations and supervises the entire functioning of a stock exchange.

To rationalize the functioning of the stock exchanges during the year 2007 all the exchanges in India were de-mutualised under a compulsory scheme brought out by SEBI in the year 2005. Except NSE all other exchanges were managed by the brokers who were members of the

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ex- change by having major stake in the composition of the Governing Board. After the demutualisation, management of the exchange rests with the owners (non-brokers) with more

Than 50% representation in the board and minority representation of the Trading Members and SEBI nominees. All the exchanges have become from not-for profit organization to that of for-profit organizations. Those exchanges which have failed to complete the de-mutualisation within the stipulated time frame as given by SEBI were cancelled of their re-cognition as an exchange and hence, they have lost their identity as exchange and cease to exist.

Trading System

Trading on stock exchanges is done through brokers and dealers. All members can act as brokers and for this purpose they have to maintain a minimum security deposit and additional security deposit also called as base capital which will decide on the trading exposure that the said broker will be allowed to. Brokers act as agents for buying and selling on behalf of their clients, for which they receive brokerage/commission at stipulated rates. The maximum brokerage that can be charged is restricted to 2.5% of the value of transaction done and there is no minimum stipulated but it cannot be nil, except when the transactions are done for charitable organizations. Dealers act as principals and buy and sell securities on their own accounts. However, members cannot enter into contract with any person other than the member without prior permission of the governing body. The Trading system of NSE has enhanced its efficiency, liquidity and transparency, by introducing a nationwide on-line fully-automated screen based trading system (SBTS) (Fig.4.1) where a member can input into the computer trading terminal, the quantities of the securities he wanted to buy or sell and the prices at which he likes to transact and the transaction is executed as soon as it finds a matching sale or buy order from a counterparty.

SBTS electronically matches orders on a strict price/time priority and hence cuts down on time, cost and risk of error, as well as on fraud resulting in improved operational efficiency. It allows faster incorporation of price sensitive information into prevailing prices, thus increasing the informational efficiency of markets. It enables market participants, irrespective of their geographical locations, to trade with one another simultaneously, improving the depth and liquidity of the market. It provides full anonymity by accepting orders, big or small, from members without revealing their identity, thus providing equal access to everybody. It also provides a perfect audit trail, which helps to resolve disputes by logging in the trade execution process in entirety.

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In the very first year of its operation, NSE became the leading stock exchange in the country, impacting the fortunes of other exchanges and forcing them to adopt SBTS also. Today India can boast that almost 100% trading take place through electronic order matching. Technology was used to carry the trading platform from the trading hall of stock exchanges to the premises of brokers.

NSE carried the trading platform further to the PCs at the residence of investors through the Internet and to handheld devices through WAP for convenience of mobile investors. This made a huge difference in terms of equal access to investors in a geographically vast country like India. The trading network is depicted in the figure.

NSE has main computer which is connected through Very Small Aperture Terminal (VSAT) installed at its office. The main computer runs on a fault tolerant STRATUS mainframe computer at the Exchange. Bro- kerbs have terminals (identified as the PCs in the Figure) installed at their premises which are connected through VSATs/leased lines/modems. An investor informs a broker to place an order on his behalf. The broker enters the order through his PC, which runs under Windows NT and sends signal to the Satellite via VSAT/leased line/modem. The signal is directed to mainframe.
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National Stock Exchange of India Ltd

The National Stock Exchange of India Limited (NSE) was promoted by IDBI, ICICI, IFCI, GIC, LIC, State Bank of India, SBI Capital Markets Limited, SHCIL and IL & FS as a Joint Stock Company under the Companies Act, 1956, on November 27, 1992. The Government of India has granted recognition with effect from April 26, 1993, initially for a period of five years. The GOI has appointed IDBI as a lead promoter. To form the infrastructure of NSE, IDBI had appointed a Honking Bound consulting firm M/s. International Securities Consulting Limited

For helping in setting up of the NSE The main objective of NSE is to ensure comprehensive nationwide securities trading facilities to investors through automated screen based trading called NEAT and automatic post trade clearing and settlement facilities. The NSE encourages corporate trading members with dealer networks, computerised trading and short settlement cycles. It has three segments, one dealing with wholesale debt instruments, the second to deal with capital market instruments called cash segment and the third for Futures and Options or Derivatives Market. The Clearing Corporation of India Limited (CCIL) an Electronic Clearing and Depository System (ECDS) set up by the Stock Holding Corporation of India Limited (SHCIL) provides the requisite clearing and settlement systems.

Features The recommendations of the High Power Committee on setting up of the National Stock Exchange, a ‘Model Exchange’ at New Mumbai to act as a National Stock Exchange (NSE) to provide access to all investors from across the country on an equal footing, and work as Integral component of the National Stock Market System. Hence, NSE is having the follow- in vital features:

➤ NSE is promoted by Financial Institutions, Mutual Funds, and financed on a self-sustain- in basis through levy of membership fees. The capital outlay of 30 cores of rupees was financed by admitting 1,000 members with an entry fee of Rs. 10 laths each. Fees for corporate and Institutional members were at a higher level of Rs. 25 laths.

➤ NSE is a company incorporated under the Companies Act of 1956. It is constituted by the Board of Directors (Board) and managed by it. 50 per cent of the Managing Board of the Exchange comprise of professionals who are not members. These professionals must be from a cross section of finance and industry, and must actively contribute to ensuring that the stock exchange functions in a balanced and fair manner.

➤ It is trading on large & medium sized securities of equity shares and debt instruments.

➤ It is a separate ring altogether. For the first time in our country, debt instruments were traded to become an active part in the secondary market of the nation.
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- NSE made its debut with the debt market. The debt market is predominantly a market in Government Securities. The Central Government moving over to auctions at market-relisted rates of interest, the primary market has become active with the well informed and fine-tuned bidding at the auctions.

- It is having full support from the National Clearing and Settlement divisions, SHCIL and the Securities Facilities Support Corporation. It is using modern computer technology for the clearance and settlement procedures.

- Better transparency system for the securities trading & settlement.

The BSE is also providing similar facilities with more number of securities being listed especially low capital companies with limited equity shares floating in the market. Both BSE and NSE has national presence and they dominate the stock markets. All other exchanges have created a platform by having either an alliance with or cross holding with these two premier exchanges or trading facility provided to their members through a subsidiary of the main exchanges.

Over the Counter Exchange of India (OTCEI)

Indeed in mid-eighties itself the G.S. Patel Committee on Stock Exchange reforms and the Abid Holi Committee on Capital Markets had recommended for the creation of a second tier stock market that will solve some of the problems of present stock exchanges. Over The Counter Exchange of India (OTCEI) was been promoted by ,JTI, IDBI, IFCI, LIC, GIC, SBI Capital Market and Canbank Financial Services as a non profit-making company under Section 25 of the Companies Act, 1956. The OTCEI is a recognized Stock Exchange under section 4 of the Securities Contracts (Regulation) Act, 1956. Hence companies listed on the OTC Exchange enjoy the same status as companies listed on any other stock exchanges in the country.

OTC Exchange of India has picked the model from the NASDAQ system (National Association of Security Dealers-Automated Quotations) prevalent in the United States of America. Modifications suited to Indian conditions been adopted from OTC in America was an offshoot of their government’s efforts to regulate the unlisted securities act. The Indian version of NASD-National Associations of Securities Dealers is what is called OTC Exchange of India. Unlike in the regular exchange, listing on OTCEI is a national listing from day one. Wherever and whenever counters start operating in the country they can trade in all the scripts of OTCEI. Separate listing in those regular places is not needed at all.
All said and done the OTCEI did not take off and was not successful due to many reasons like lower end technology, low liquidity, less participation by investors in small cap companies, etc.

Inter-connected Stock Exchange of India

Inter-connected Stock Exchange of India Limited (ISE) has been promoted by 15 Regional stock exchanges to provide trading linkage/connectivity to all the participating exchanges to widen their market. Thus, ISE is a national level exchange providing trading, clearing, settlement, risk management and surveillance support to the Inter-Connected Market System (ICMS). ISE aims to address the needs of small companies and retail investors with the guiding principle of optimising the infrastructure and harnessing the potential of regional markets to transform these into a liquid and vibrant market through the use of technology and networking. The participating exchange in ISE has in all about 4500 traders. In order to leverage it's infrastructure as also to expand its nation-wide reach, ISE has also appointed dealers across various cities other than the participating exchange centres. These dealers are administratively supported through strategically located regional offices at Delhi, Calcutta, Chennai and Nagpur.

ISE thus expects to emerge as a low cost national level exchange in the country for retail investors and small intermediaries. ISE has also floated a wholly-owned subsidiary namely, ISE Securities and Services Limited (ISS) to take membership of NSE and other premier exchanges, so that traders and dealers of ISE can access other markets in addition to the local market and ISE. This will provide the investors in smaller cities with a solution for cost-effective and efficient.

Client trading in securities.

Core objectives of the Inter-connected Stock Exchange include creation of single integrated national level solution with access to multiple markets for providing high quality, low cost services to millions of investors across the country, a liquid and vibrant national level market for all listed companies in general and small capital companies in particular and providing trading, clearing and settlement facilities to the traders and dealers across the country at their doorstep with decentralised support system. Some of the features which make ISE a new age stock exchange are as follows:

- ISE is a national level recognised stock exchange having moderate listing fees and granting listing and trading permission to small and medium sized companies having a post public issue paid-up capital of Rs. 3 crore to Rs. 5 crore (subject to the appointment of market makers) besides companies with a capital of above Rs. 5 crore.
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- All traders and dealers of ISE have access to NSE through ISE Securities and Services Ltd. (ISS), which ensures continuous attention of investors.
- Proposing to introduce the 'IPO Distribution System' for offering primary market issue.
- ISE has set up an 'Investors Grievance and Service Cell' which looks after all types of complaints of investors located across the country and provides decentralised support.
- Listing of stocks with ISE would give the company an advantage of being identified as a technology-savvy and investor-friendly company.

Demutualization of Stock Exchanges

Historically stock exchanges were formed as 'mutual' organisations, which were considered beneficial in terms of tax benefits and matters of compliance. They are generally 'not-for-profit' and tax-exempted entities. The trading members who provide broking services, also own, control and manage such exchanges for their common benefit, but do not distribute the profits among themselves.

The ownership rights and trading rights are clubbed together in a member-ship card which is not freely transferrable and hence this card at times carries a premium. In contrast, in a 'demutual' exchange, three separate sets of people own the exchange, manage it and use its services. The owners usually vest in management constituting a board of directors which is assisted by a professional team.

A completely different set of people use trading platform form of the exchange. These are generally 'for-profit' and taxpaying entities. The ownership rights are freely transferrable. Trading rights are acquired/surrendered in terms of transparent rules. Membership cards do not exist. These two models of exchanges are generally referred to as 'club' and 'institution' respectively.

There are 23 recognised exchanges in the country. Three of them are 'Association of Persons', while the balance 20 are companies, either limited by guarantee or by shares. Except one exchange (NSE), all exchanges, whether corporate or association of persons, are not-for-profit making organisations. Except for two (OTCEI and NSE), all exchanges are 'mutual' organisations.

An expert committee appointed by SEBI has recently recommended demutualisation of stock exchanges since stock exchanges, brokers, associations and investors association have overwhelmingly felt that such a measure was desirable. The committee has accordingly suggested the steps for such demutualisation.

The most important development in the capital market is concerning the demutualisation of the stock exchanges. Demutualisation of exchanges means segregating the ownership from

Researcher: CVSL Kameswari
management. This move was necessitated by the fact that brokers in the management of the stock exchange were misusing their position for personal gains.

Demutualisation would bring in transparency and prevent conflict of interest in the functioning of the stock exchanges. The Minister of Finance in his union budget speech of 2002-03 has made important announcement that the process of demutualisation and corporatisation of stock exchanges is expected to be completed during the course of the current year.

Now, all the stock exchanges in India are demutualised entities

**Development Initiatives**

**Continued Reforms Process in Primary Market:** Continued reforms in the primary market further strengthened investors' confidence.

Following were the major policy initiatives taken by SEBI relating to the primary market:-

**i. Encouragement of Retail Investor Participation:**

In order to increase retail investor participation and to keep pace with inflation, monetary limit on retail individual investor application was increased from Rs.1 lakh to Rs.2 lakh. The limit was enhanced with the objective that retail individual investors who have capacity and appetite to apply for securities worth above Rs.1 lakh should not be constrained.

**ii. Reforms in Issue Process**

In order to make our markets competitive, SEBI has been constantly reviewing various rules and procedures to make issue process simpler and at the same time safer. Some of the major initiatives in this area include:

a. **Reduction in process time lines:** In order to lessen the market risk, infrastructural stress and costs, time between issue closure and listing was reduced from 22 days to 12 working days. Reduction in process timelines help in reducing exposure of issuers/ investors to volatility in market conditions, enable quicker turnaround of money invested and help issuers to raise money quicker.

b. **Enhancement in Application Supported by Blocked Amounts (ASBA) Process:** To smoothen the payment/refund process in issues, SEBI has introduced Applications Supported by Blocked Amount (ASBA) Process in issues, wherein application money is blocked in a bank.
account and debited only to the extent of allotment entitlement while continuing to earn interest. ASBA has resulted in the following benefits:

2010-11

During financial year 2010-11, the primary market had been quite active with overwhelming response to Initial Public Offers (IPOs).

In FY 2010-11, 61 public issues hit the market of which only 20 are trading above their issue prices. That is, only 33 per cent of issues. And, about 41 companies are producing negative returns.

That is, two thirds of the public issues are trading below their issue prices. Though there was huge discrepancy between the post listing price and IPO price, SEBI through its quick and rapid investigations has penalized some of the erring merchant bankers in 2011-12, which lead to the banning of those merchant banking entities from raising resources from capital markets.

Some of the Public Issues which lead to SEBI action have been depicted in the below diagram. Given the fact that Regulatory is active and taking timely action, Investors post 2011 scenario, have become quite alert and only good issues with good pedigree and established merchant bankers are only finding subscriptions in the current market scenario even.
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Figure 5: IPO Gains or Losses: FY2010-11

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Initiatives and developments in SEBI in Indian Securities Market in the year 2010

January 2010  SEBI allowed stock exchanges to introduce currency futures on additional currency pairs — GBP-INR EUR-INR and JPY-INR.

February 2010  SEBI set up committee for review of ownership and governance of market infrastructure institutions

April 2010  Reduction in time between issue closure and listing

May 2010  Introduction of Index options with tenure up to 5 years

May 2010  Permitting to set up a Stock exchange/ a trading platform by a recognized stock exchange having nationwide trading terminals for SME

July 2010  Introduction of call auction in Pre-open session.

July 2010  Allowing Physical Settlement of Stock Derivatives

July 2010  Market Access through Authorised Persons

July 2010  Reporting of OTC transactions in Certificates of Deposit (CDs) and Commercial Papers (CPs)

August 2010  Introduction of Smart Order Routing

August 2010  SEBI allows securities trading using wireless technology

October 2010  European Style Stock Options

October 2010  Currency Options on USD-INR were allowed for trading at NSE.

November 2010  Facilitating transactions in mutual fund schemes through the Stock Exchange infrastructure.

Secondary market witnessed volatility amidst adverse developments in global financial markets. The initial positive headways fizzled out as global markets became increasingly adverse owing to Euro-zone debt crisis at the start and Middle East and North African crisis in later half of the year. Following were the major policy initiatives taken by SEBI relating to the secondary market during 2010-11:

Guidelines for Market Makers on Small and Medium Enterprise (SME) Exchange/ Separate Platform of Existing Exchange having Nationwide Terminal

SEBI put in a framework for setting up of new exchange/separate platform of existing stock exchange having nationwide terminals, for SME. In order to operationalize the said framework, SEBI vide circular dated April 26, 2010, issued guidelines on Market Making for SME.

Foreign Institutional Investors (FIIs) Permitted to Offer Domestic Government Securities as Collateral for Margins

Reserve Bank of India (RBI) vide A. P. (DIR Series) Circular no. 47 dated April 12, 2010, permitted FIIs to offer domestic Government securities and foreign sovereign securities with AAA rating, as collateral to the recognised stock exchanges in India, in addition to cash, for their
transactions in the cash segment of the market. However, SEBI has specified that cross-margining of Government securities (placed as margins by the FIIs for their transactions in the cash segment of the market) shall not be allowed between the cash and the derivative segments of the market.

Account Maintenance Charges (AMC) Collected Upfront on Annual/Half Yearly Basis on Demat Accounts by Depository Participants

In the interest of investors, SEBI vide circular no. MRD/DP/20/2010 dated July 1, 2010 informed that in the event of closing of the demat account or shifting of the demat account from one DP to another, the AMC collected upfront on annual/half yearly basis by the DP, shall be refunded by the DP to the BO for the balance of the quarter/s.

Call Auction in Pre-open Session

SEBI vide circular dated July 15, 2010, introduced call auction in pre-open Session on a pilot basis for securities forming part of Sensex and Nifty. The call auction mechanism is expected to reduce volatility and aids in better price discovery.

Mandatory Requirement of PAN

In order to ensure better compliance with the Know Your Client (KYC) norms, it was informed that with effect from August 16, 2010, PAN non-compliant demat accounts would also be “suspended for credit” other than the credits arising out of automatic corporate actions. It was clarified that other credits including credits from IPO/FPO/Right issue, off-market transactions or any secondary market transactions shall not be allowed into such accounts.

Securities Trading Using Wireless Technology

SEBI registered brokers who provide internet based trading as specified by SEBI circular dated January 31, 2000 shall be eligible to provide securities trading using wireless technology. All relevant requirements applicable to internet based trading shall also be applicable to securities trading using wireless technology.

Smart Order Routing

Based on the proposal received from stock exchanges and market participants and the recommendation of TAC, SEBI has introduced the facility of Smart Order Routing (SOR) which allows the brokers trading engines to systematically choose the execution destination based on factors viz. price, costs, speed, likelihood of execution and settlement, size, nature or any other consideration relevant to the execution of the order. This facility would help brokers execute...
client orders efficiently by providing the best price available across multiple trading venues (stock exchanges).

**Securities Lending and Borrowing Mechanism (SLB)**

Further to extending the contract tenure for securities lending and borrowing, from a period of 30 days to a maximum period of 12 months and providing the facility of early recall and repayment of securities, it was specified vide circular dated October 7, 2010 that, dividend amount would be worked out and recovered from the borrower on the book closure/record date and passed on to the lender.

**Change in Activity Schedule for T+2 Rolling Settlement (Auction Schedule)**

In order to reduce the time involved in delivering the shares to the buying broker, in case of default by the selling broker, SEBI vide circular dated December 28, 2010, revised the auction schedule, to be conducted on the same day of the settlement, after the pay-in is completed i.e. the auction for trades done on T day shall be conducted on T+2 day after pay in is completed and shortfall is crystallized. The settlement of the same would be carried out on T+3 day.

**Policy Initiatives for Derivatives**

**a) Exchange Traded Currency Derivatives:**

SEBI, vide circular dated January 19, 2010, permitted exchanges to introduce currency futures on Euro-INR, Pound Sterling-INR and Japanese Yen-INR. Futures on these currency pairs were introduced at NSE and MCX-SX on February 1, 2010 and at USE on September 20, 2010.

**b) Derivative Contracts on Volatility Index:**

SEBI, vide circular dated April 27, 2010, permitted stock exchanges to introduce derivative contracts on Volatility Index, subject to the condition that the underlying Volatility Index has a track record of at least one year and the exchange has in place appropriate risk management framework for such derivative contracts. Stock exchanges disseminate data on Volatility Index on a regular basis.

**c) Physical Settlement of Stock Derivatives:**

SEBI, vide circular dated July 15, 2010, provided stock exchanges flexibility to offer; (i) cash settlement (settlement by payment of differences) for both stock options and stock futures; or (ii) physical settlement (settlement by delivery of underlying stock) for both stock options and stock futures; or (iii) cash settlement for stock options and physical settlement for stock futures; or (iv) physical settlement for stock options and cash settlement for stock futures.
d) Options on USD-INR Spot Rate:

SEBI, vide circular dated July 30, 2010, permitted stock exchanges to introduce options on USD-INR spot rate in their currency derivatives segment. Options on USD-INR were introduced at NSE and USE on October 29, 2010.

e) European Style Stock Options:

SEBI, vide circular dated October 27, 2010, provided stock exchanges flexibility to offer either European style or American style stock options. After opting for a particular style of exercise, a stock exchange has to offer option contracts of the same style on all eligible stocks. European style stock options were introduced at NSE for all options contracts expiring on or after January 27, 2011 and at BSE for contracts expiring on or after March 17, 2011.

f) Derivative Contracts on Foreign Stock Indices:

SEBI, vide circular dated January 11, 2011, permitted stock exchanges to introduce derivative contracts (Futures and Options) on foreign stock indices in their equity derivatives segment.

g) Interest Rate Futures:

SEBI, vide circular dated March 7, 2011, permitted stock exchanges to introduce Futures on 91-day Government of India Treasury-Bill (T-Bill) in their currency derivatives segment.

Committee for Review of Ownership and Governance of Market Infrastructure Institutions (MIIs)

A committee, under the Chairmanship of Dr. Bimal Jalan (former Governor of Reserve Bank of India), had been constituted to examine the issues arising from the ownership and governance of Market Infrastructure Institutions. The committee has submitted its final report on November 22, 2010 and the same is disseminated at SEBI website for public comments.

Disclosure of Regulatory Orders and Arbitration Awards on Stock Exchange Website

Based on the feedback and inputs received from investor associations, it was informed vide circular dated April 1, 2010 that stock exchanges shall post all their regulatory orders and arbitration awards issued since April 1, 2007, on their websites within 30 days. Further, all regulatory orders and arbitration awards as and when issued by exchanges from the date of this circular, shall be posted on their websites immediately.
Setting Up of a Stock Exchange/ a Trading Platform by a Recognised Stock Exchange having Nation-wide Trading Terminals for Small and Medium Enterprise (SME)

SEBI vide circular dated May 18, 2010 has put in place the framework for recognition and supervision of SME. A company desirous of being recognised as a SME exchange or a recognised stock exchange having nationwide trading terminals desirous to set up a trading platform may apply to SEBI, in accordance with the provisions of the Securities Contracts (Regulation) Act, 1956 read with the provisions of the Securities Contracts (Regulation) Rules, 1957, subject to the applicant fulfilling the conditions, interalia, stipulates i.e. it shall be a corporatized & demutualised entity, compliant with Securities Contracts (Regulation) (Manner of Increasing and Maintaining Public Shareholding in Stock Exchanges) Regulations, 2006, have balance sheet net-worth of at least Rs.100 crore, have online surveillance capability, it shall have adequate arbitration and investor grievance redressal mechanism. The minimum lot size for the trading on the stock exchange shall be one lakh rupees.

Arbitration Mechanism in Stock Exchanges

SEBI, vide circulars dated August 11, 2010, August 31, 2010 and February 09, 2011 has streamlined the arbitration mechanism available at stock exchanges for arbitration of disputes arising between a client and a member across various market segments. A stock exchange shall provide an arbitration mechanism for settlement of disputes between a client and a member through arbitration proceedings. The abovementioned circulars inter-alia stipulate the criteria for panel of arbitrators, code of conduct for arbitrators, time period for passing/implementation of the arbitral award/appellate arbitral award, limitation period in terms of Limitation Act, 1963, appellate arbitration mechanism in the stock exchange, uniformity in arbitration fees, place of arbitration, competent court, and maintenance of records and disclosures.

Mandating the Stock Exchanges to credit the penalties levied on their members to their Investor Protection Fund

Stock exchanges were earlier treating the penalties levied on their member brokers as their revenue. SEBI vide letter dated June 25, 2010 advised all the stock exchanges to credit the penalties levied by them on their members to their Investor Protection Funds (IPFs). Amongst the active stock exchanges, NSE, MCX-SX, CSE and MSE have already complied with the requirement of crediting penalties levied on their members to their IPFs. However, BSE is in the process of carrying out necessary amendments to its byelaws, pursuant to which it will comply with the requirement. The aggregate amount of penalties transferred by the stock exchanges during the year 2010-11 to IPFs was Rs.7.26 lakh.
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Display of Details by Stock Brokers

It was observed that the stock brokers were making prominent use of brand names/ logos of their group companies instead of using their names as registered with SEBI. This was creating confusion in the minds of the investors. Hence, SEBI vide circular dated November 4, 2010 advised the stock brokers that while a stock broker may use the brand name / logo of its group companies, it must display the following more prominently:

a) its name as registered with SEBI, its own logo, if any, its registration number, and its complete address with telephone numbers in its portal /web site, if any, notice / display boards, advertisements, publications, know your client forms, and member client agreements;

b) its name as registered with SEBI, its own logo, if any, its registration number, and its complete address with telephone numbers, the name of the compliance officer, his telephone number and e-mail address in the contract notes, statement of funds and securities, and correspondences with the clients. This will help the clients to contact the compliance officer of the stock broker in case of any complaints or if any information is required.

Enhancing the Competency Level of the Employees of the Market Intermediaries

a) Certification of Approved Users and Sales Personnel of the Trading Members of the Currency Derivatives Segment Trading in Interest Rate Derivatives

SEBI vide notification dated June 29, 2010 mandated the requirement of series-IV: IRD certification for approved users and sales personnel of the trading members of currency derivatives segment trading in interest rate derivatives. This will ensure that the persons employed by the trading members are certified and thus they will be better equipped to carry out the dealing and sales operations skilfully and effectively.

b) Certification of Persons Associated with Registered Stock Brokers Involved in Risk Management

SEBI vide notification dated December 10, 2010 mandated the requirement of NISM-Series-VII: Securities Operations and Risk Management Certification for persons associated with a registered stock-broker /trading member/ clearing member in recognised stock exchanges, who are involved in, or deal with assets or funds of investors or clients, redressal of investor
grievances, internal control or risk management, or activities having a bearing on operational risk. This will enable them to discharge their responsibilities effectively in the interest of investors.

c) Certification of Associated Persons of Registered Depository Participants

SEBI vide notification dated March 29, 2011 mandated the requirement of NISM-Series-VI: Depositories Operations Certification Examination (DOCE) for associated persons engaged or employed or to be engaged or employed by a registered Depository Participant. An associated person is one who is responsible for dealing or interacting with clients, dealing with securities of clients, handling redressal of investor grievances, internal control or risk management, activities having a bearing on operational risk or maintenance of books and records pertaining to the above activities. This will equip them to discharge their responsibilities effectively in the interest of investors and market.

Expansion of Market Access through Authorised Persons

With a view to expand the reach of the markets for exchange traded products, SEBI vide circular dated November 6, 2009 had allowed registered stock brokers to provide market access to clients through Authorised Persons (APs) and provided a broad framework governing the same. Further, vide circular dated July 23, 2010 the certification requirements for APs were rationalized in line with those applicable for stock brokers and sub-brokers. As of March 31, 2011, 63,042 APs have been registered by the stock exchanges, as against 34,767 as on March 31, 2010. Thus, there has been a substantial increase in the number of APs registered with the stock exchanges and thus increasing the reach of the markets for exchange traded products.

Granting of Permanent Registration to Intermediaries

According to Regulations, while the stock brokers and sub-brokers are granted permanent registration, other intermediaries are granted registration for a period of 3 – 5 years. After the expiry of their registration, the above intermediaries, if they so desire, apply for renewal in order to continue their business. The purpose of renewal is to check whether the intermediary is complying with the basic requirements such as net-worth, infrastructure, key personnel, fit and proper compliance, etc. Apart from renewal, other checks and balances are available with SEBI for monitoring the activities of the intermediaries on a continuous basis. Accordingly, SEBI Board approved the proposal to amend the respective Regulations governing the intermediaries to grant permanent registration to the intermediaries. The intermediaries would be granted registration initially for a period of five years. On assessment of the performance of the intermediary and its track record during the initial five years, it will be granted registration on
permanent basis. Necessary amendments to the regulations are being carried out. The above would streamline the registration process and help SEBI in effective regulation of intermediaries.

Dispensed with Prior Approval (Except for Change in Control)

It was decided to do away with the requirement of obtaining prior approval from SEBI by the intermediaries for 'change of their status or constitution' as defined in the regulations. SEBI receives a lot of such requests in respect of very small and sometimes insignificant changes in the constitution of the intermediaries. It was felt desirable that the time spent on these activities can be focused on inspection and monitoring of intermediaries and their effective regulation. However, in case of change in control, the intermediaries except the sub-brokers -who do not deal with funds and securities of clients - would continue to seek prior approval of SEBI. SEBI Board approved the proposal and necessary amendments to the regulations are being carried out.

Enhanced Transparency and Disclosure Norms for Credit Rating Agencies (CRAs)

Recent events in global financial system have underlined the pivotal role that credit rating agencies play in the financial sector. Effective use of credit ratings by the users is crucially dependent upon quality and quantity of disclosures made by the Credit Rating Agencies (CRAs). There have been widespread consultations on the issue both globally and within India and several documents have been prepared. In the wake of the above and in order to impart higher credibility to the processes and procedures associated with the credit rating, SEBI prescribed the following norms for transparency and disclosures in consultation with the CRAs:

a. Rating Process

A CRA shall, in support of each credit rating and review / surveillance thereof, keep till five years after maturity of instruments, the records of:

i. The important factors underlying the credit rating and sensitivity of such credit rating to changes in these factors;

ii. Summary of discussions with the issuer, its management, auditors and bankers which have a bearing on the credit rating;

iii. Decisions of the rating committee(s), including voting details and notes of dissent, if any, by any member of the rating committee.

iv. In case of a quantitative model being a substantial component of the credit rating process, the rationale for any material difference between the credit rating implied by the model and the credit rating actually assigned.
b. Default Studies

In order to promote transparency and to enable the market to best judge the performance of the ratings, the CRA, shall publish information about the historical default rates of CRA rating categories and the changes in the default rates of these categories over time. For this purpose, the method for calculation of one-year default rate as well as cumulative default rate has been specified. On annual basis, the average one-year and three-year cumulative default rates(based on weighted average), for the last 5 years, shall be disclosed for each credit rating category as well as structured and non-structured instruments, separately.

c. Dealing with Conflict of interest

For dealing with the conflict of interests, the CRAs shall formulate the policies and internal codes and ensure that

(a) Its analysts do not participate in any kind of marketing and business development including negotiations of fees with the issuer, whose securities are being rated,

(b) The employees’ involved in the credit rating process and their dependants do not have ownership of the shares of the issuer and there is a prompt review of the credit ratings of the securities as and when any of its employees joins the respective issuer.

d. Obligations in Respect of Rating of Structured Finance Products

In case a CRA undertakes rating of structured finance products, namely, instruments / pay-outs resulting from securitisation transactions, the CRA or its subsidiaries shall not provide consultancy or advisory services regarding the design of the structured finance instrument. Also that the rating symbols shall clearly indicate that the ratings are for structured finance products.

While publishing the ratings of structured finance products and their movements, the track record of the originator and details of nature of underlying assets while assigning the credit rating also needs to be disclosed.

e. Unsolicited Credit Ratings

In case of unsolicited credit ratings, i.e. the credit ratings not arising out of the agreement between a CRA and the issuer, credit rating symbol shall be accompanied by the word “UNSOLICITED” in the same font size. The CRA is required to monitor and disclose credit rating during the life of the rated securities, as if it were a solicited rating. The CRAs shall disclose annually all the unsolicited ratings carried out in the last three financial years.
f. Disclosure of Information

The CRAs are required to make the following disclosures to bring about transparency in their operations:

- A CRA shall disclose on its website the rating procedure, Credit rating history and defaults, income, structured finance products, unsolicited credit ratings, shareholding and compliance status of IOSCO Code of Conduct. A CRA shall formulate and disclose its policies, methodology and procedures in detail regarding solicited and unsolicited credit ratings. A CRA shall disclose the details of new credit ratings assigned as well the movement of the outstanding ratings.

- In case of listed securities, the CRA shall also make disclosures to the stock exchanges as specified in the SEBI (Credit Ratings) Regulations, 1999. For ratings assigned and their periodic reviews, the CRA shall issue press releases which shall also be placed on their websites.

- The CRAs are required to disclose the general nature of its compensation arrangements with the issuers along with the details of conflict of interest with the issuer, if any, and annual disclosure of its total receipt from rating services and non-rating services.

- The half-yearly disclosures stipulated above shall be made by the CRAs within 15 days from the end of the half year (March / September). The yearly disclosures stipulated above shall be made by the CRAs within 30 days from the end of the financial year.

Constitution of Standing Committee for Credit Rating Agencies

The CRAs registered with SEBI also carry out rating of securities and instruments not arising out of public or rights issues which are relied upon by other regulators and investors. In order to bring about coordination among the regulators pertaining to issues related to CRAs, a Standing Committee comprising of representatives of all the regulators (SEBI, RBI, IRDA & PFRDA) has been set up. The Committee met twice during the financial year and discussed various issues related to CRAs.

Conclusion

The regulatory agency has been quite actively pursuing for the development of both primary and secondary market while strengthening the regulation from time to time to avoid any contingent spillovers. Today India can boast one of the best regulated financial markets in the world thanks to SEBI. Indian Markets are the well-regulated markets when compared to any other markets in the world as per the Economist Magazine.