
STUDY MATERIAL

EXECUTIVE PROGRAMME

CAPITAL MARKETS

AND

SECURITIES LAWS

MODULE II

PAPER 6



**THE INSTITUTE OF
Company Secretaries of India**

IN PURSUIT OF PROFESSIONAL EXCELLENCE

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EXECUTIVE PROGRAMME

CAPITAL MARKETS AND SECURITIES LAWS

The Indian Capital market has grown exponentially in terms of resource mobilization, number of listed stocks, market capitalization, trading volumes, and investors' base. Along with this growth, the profiles of the investors, issuers and intermediaries have changed significantly. The market has witnessed a fundamental institutional change resulting in drastic reduction in transaction costs and significant improvement in efficiency, transparency and safety. The measures taken by SEBI such as, market determined allocation of resources, rolling settlement, sophisticated risk management and derivatives trading have greatly improved the framework and efficiency of trading and settlement, making the Indian capital market qualitatively comparable to many developed markets.

This study material has been published to aid the students in preparing for the Capital Market and Securities Laws paper of the CS Executive Programme. It is part of the educational kit and takes the students step by step through each phase of preparation stressing key concepts, pointers and procedures. Company Secretaryship being a professional course, the examination standards are set very high, with emphasis on knowledge of concepts, applications, procedures, for which sole reliance on the contents of this study material may not be enough. Besides, as per the Company Secretaries Regulations, 1982, **students are expected to be conversant with the amendments to the laws made upto six months preceding the date of examination.** The material may, therefore, be regarded as the basic material and must be read alongwith the original Bare Acts, Rules, Regulations, Academic Guidance etc. This study has been updated upto October, 2017.

The subject of Capital Market and Securities Laws is inherently complicated and is subject to constant refinement through new primary legislations, rules and regulations made thereunder. It, therefore becomes necessary for every student to constantly update himself with the various legislative changes made from time to time by referring to the Institute's journal 'Chartered Secretary' as well as other professional journals.

In the event of any doubt, students may write to the Directorate of Studies for clarification at **academics@icsi.edu**.

Although care has been taken in publishing this study material yet the possibility of errors, omissions and/or discrepancies cannot be ruled out. This publication is released with an understanding that the Institute shall not be responsible for any errors, omissions and/or discrepancies or any action taken in that behalf.

Should there be any discrepancy, error or omission noted in the study material, the Institute shall be obliged if the same is brought to its notice.

This study material is based on those sections of the Companies Act, 2013 and the rules made there under which have been notified by the Government of India and came into force w.e.f. April 01, 2014.

SYLLABUS

PAPER 6: CAPITAL MARKETS AND SECURITIES LAWS (100 Marks)

Level of Knowledge: Expert Knowledge

Objective: *To acquire knowledge and understanding of securities laws and the regulatory framework of capital markets.*

Contents:

Part A: Capital Markets (60 Marks)

1. Overview of Capital Market

- Indian Capital Market
- Authorities Governing Capital Markets in India
- Profile of Securities Market
- Securities Market Reforms and Regulatory Measures to Promote Investor Confidence
- Features of Developed Capital Market: IOSCO
- Overview of Depository System in India

2. Capital Market Instruments and Rating

- Capital Market Instruments: Equity, Debentures, Preference Shares, Sweat Equity, Non-Voting Shares, Share Warrants
- Pure, Hybrid and Derivatives
- Rating and Grading of Instruments: Concept, Scope and Significance, Regulatory Framework
- Rating Agencies in India, Rating Methodologies

3. Securities Market Intermediaries

- Primary Market and Secondary Market Intermediaries: Role and Functions, Merchant Bankers, Stock Brokers, Syndicate Members, Registrars, Underwriters, Bankers to an Issue, Portfolio Managers, Debenture Trustees, Foreign Institutional Investors, Depositories, Depositories Participants, Custodians, Credit Rating Agencies, Venture Capitalists

4. Market Infrastructure Institutions - Stock Exchanges

- Functions and Significance of Stock Exchanges
- Operations and Trading Mechanism of Stock Exchanges
- Settlement of Securities, Stock Market Indices, Risk Management, Surveillance Mechanism at Stock Exchanges, Straight through Processing
- Demutualization of Stock Exchanges
- SME Exchange

5. Debt Market

- Debt Market: Instruments, Listing, Primary and Secondary Segment

6. Money Market

- Growth of Money Market in India – Structure and Institutional Mechanism

- Money Market Instruments: Treasury Bills, Commercial Bills, Commercial Paper, Factoring Agreements & Discounting of Bill

7. Mutual Funds

- Mutual Fund: Introduction, Definitions, Schemes, Risks Involved, Setting Up of Mutual Funds, Role in Financial Market
- Advantage of Investment in Mutual Fund
- Concept of Trustee and Asset Management Company
- Legal & Regulatory Framework
- Offer Document, Accounting Valuation & Taxation
- Investment Management: Equity & Debt Portfolio, Measuring & Evaluating Mutual Fund Performance
- Investor's Rights and Obligations

8. Venture Capital

- Concept of Venture Capital
- Registration, Investment Conditions and Restrictions
- Foreign Venture Capital Investors
- Private Capital Funds

9. Collective Investment Schemes

- Regulatory Framework
- Restrictions on Business Activities
- Submission of Information and Documents
- Trustees and their Obligations

10. Resource Mobilization in International Capital Market

- Listing of Securities Issued Outside India
- Foreign Currency Convertible Bonds
- Global Depository Receipts
- American Depository Receipts
- External Commercial Borrowings
- Procedure for Issue of Various Instruments

11. Indian Depository Receipts

- Indian Depository Receipts: Procedure for Making Issue of IDRs, Conditions for Issue of IDRs, Listing of IDRs

12. Foreign Portfolio Investors

- Concept of FPIs, Registration of FPIs, Offshore Derivative Instruments (ODIs), Obligation of FPIs and DDP & Inspection & Investigation.

13. Non-Convertible Redeemable Preference Shares

- Issue and listing of Non-convertible Redeemable Preference Shares, Obligations of the Issuer and Lead Merchant Banker, Issuance & Listing of Non-Equity Regulatory Capital Instruments by Banks and Inspection and Power of SEBI.

14. Real Estate Investment Trusts

- Registration of Real Estate Investment Trusts, Rights and Responsibilities of Parties to the REIT, Valuer Sponsor and Auditor, Issue and Listing of Units, Investment conditions, related party transactions, Borrowing and valuation of assets, Rights and Meetings of Unit Holders and Disclosures

15. Infrastructure Investment Trusts

- Registration of Infrastructure Investment Trusts, Rights and Responsibilities of Parties to the InvIT, Project Manager, Sponsor, Valuer and Auditor, Offer of Units of InvIT and Listing of Units, Investment conditions, Related Party Transactions, Borrowing and valuation of assets, Rights and Meetings of Unit Holders and Disclosures

Part B: Securities Laws (40 Marks)

16. Securities Contracts (Regulation) Act, 1956

17. SEBI Act, 1992

- Objective, Power and Functions of SEBI
- Securities Appellate Tribunal, Appeals, Appearance before SAT

18. Depositories Act, 1996

- Definitions, Setting up of Depository, its type, Role and Functions
- Depository Participants
- Admission of Securities
- Difference between Dematerialization & Rematerialisation
- Depository Process
- Inspection and Penalties
- Internal Audit and Concurrent Audit of Depository Participants

19. Issue and Listing of Securities

- Listing of Securities
- Issue of Capital and Disclosure Requirements (ICDR)
- Procedure for Issue of Various Types of Shares and Debentures
- Employee Stock Option Scheme and Employee Stock Purchase Scheme
- Delisting of Securities

20. Regulatory Framework relating to Securities Market Intermediaries

- Primary Market and Secondary Market Intermediaries: Role and Functions, Merchant Bankers, Stock Brokers, Syndicate Members, Registrars, Underwriters, Bankers to an Issue, Portfolio Managers, Debenture Trustees, Foreign Institutional Investors, Custodians, Credit Rating Agencies, Venture Capitalists

21. An Overview of Law relating to Insider Trading and Takeovers

22. Investor Protection

- Investors' Rights and Responsibilities, types of grievances and dealing authority, Investor Education and Protection Fund (IEPF) under SEBI Regulations and Companies Act, 2013, Financial Education, Investor Grievance Redressal Mechanism at SEBI etc.

LIST OF RECOMMENDED BOOKS

PAPER 6 : CAPITAL MARKETS AND SECURITIES LAWS

READINGS

1. E. Gordon & K. Natarajan : Capital Market in India; Himalaya Publishing House, Ramdoot, Dr. Bhalerao Marg, Girgaon, Mumbai - 400004.
2. Sanjeev Aggarwal : Guide to Indian Capital Market; Bharat Law House, 22, Tarun Enclave, Pitampura, New Delhi – 110 034.
3. V.L. Iyer : SEBI Practice Manual; Taxman Allied Service (P) Ltd., 59/32, New Rohtak Road, New Delhi-110005.
4. M.Y. Khan : Indian Financial Systems; Tata McGraw Hill, 4/12, Asaf Ali Road, New Delhi – 110 002.
5. S. Suryanarayanan & V. Varadarajan : SEBI – Law, Practice & Procedure; Commercial Law Publishers (India) Pvt. Ltd., 151, Rajindra Market, Opp. Tis Hazari Court, Delhi - 110054
6. Mamta Bhargava : Compliances and Procedures under SEBI Law; Shreeji Publishers, 8/294, Sunder Vihar, New Delhi – 110 087
7. Taxmann : SEBI Manual
8. Asim Kumar Mishra : Venture Capital Financing in India; Shipra Publications, 115A, Vikas Marg, Shakarpur, Delhi-110092.
9. Shashi K Gupta : Financial Institutions and Markets ; Kalyani Publishers, 4863/2B, Bharat Ram Road, 24, Daryaganj, New Delhi -110002
- Neeti Gupta
10. Vishal Saraogi : Capital Markets and Securities Laws simplified, Lawpoint Publication, 6C, R.N. Mukherjee Road, Kolkata-700001

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1. SEBI Annual Report : SEBI, Mumbai.
2. Indian Securities Market - A Review : NSE Yearly Publication
3. Website : www.sebi.gov.in
www.nseindia.com
www.bseindia.com
www.rbi.org.in
www.mca.gov.in

JOURNALS

1. SEBI and Corporate Laws : Taxmann, 59/32, New Rohtak Road, New Delhi-110 005.
2. Corporate Law Adviser : Corporate Law Adviser, Post Bag No. 3, Vasant Vihar, New Delhi-110052.

3. SEBI Monthly Bulletin : SEBI, Mumbai.
4. NSE News : National Stock Exchange of India Ltd., Mahindra Towers, Worli, Mumbai-400018.

Note : Students are advised to read relevant Bare Acts and Rules and Regulations relating thereto. E-Bulletin 'Student Company Secretary' and 'Chartered Secretary' should also be read regularly for updating the knowledge.

ARRANGEMENT OF STUDY LESSONS

PART A

1. Overview of Capital Market
2. Capital Market Instruments
3. Credit Rating and IPO Grading
4. Market Infrastructure Institutions - Stock Exchange Trading Mechanism
5. Debt Market
6. Money Market
7. Mutual Funds
8. Alternative Investment Fund
9. Collective Investment Schemes
10. Resource Mobilization in International Capital Market
11. Indian Depository Receipts
12. Foreign Portfolio Investors
13. Non-Convertible Redeemable Preference Shares
14. Real Estate Investment Trusts
15. Infrastructure Investment Trusts

PART B

16. Regulatory Framework Governing Stock Exchanges
17. Securities and Exchange Board of India
18. Depositories
19. Listing and Delisting of Securities
20. Issue of Securities
21. Regulatory Framework relating to Securities Market Intermediaries
22. Insider Trading- An overview
23. Takeover Code- An Overview
24. Investor Protection

TEST PAPER

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Lesson 1

Overview of Capital Market

LESSON OUTLINE

- Introduction
- Organisational Structure of Financial System
- Functions of Securities Market
- Securities Market and Economic Growth
- A Profile of Securities Market
- Market Regulations
- Securities Market Reforms and Regulatory Measures to promote Investor Confidence
- International Organisation of Securities Commission (IOSCO)
- Overview of Depository System in India
- LESSON ROUND UP
- GLOSSARY
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LEARNING OBJECTIVES

The Capital Market is a market for financial investments that are direct or indirect claims to capital. It embraces all forms of lending and borrowing, whether or not evidenced by the creation of a negotiable financial instrument. The Capital Market comprises the complex of institutions and mechanisms through which intermediate term funds and long term funds are pooled and made available to business, government and individuals. The Capital Market also encompasses the process by which securities already outstanding are transferred.

This lesson will enable the students to understand the basics of Capital Market, the major securities market reforms taken by SEBI, the role of IOSCO in securities market regulation and the overview of depository system in India.

INTRODUCTION

Every modern economy is based on a sound financial system which helps in production, capital and economic growth by encouraging savings habits, mobilising savings from households and other segments and allocating savings into productive usage such as trade, commerce, manufacture etc.

Financial system covers both credit and cash transactions. All financial transactions are dealt with by cash payment or issue of negotiable instruments like cheque, bills of exchanges, hundies etc. Thus a financial system is a set of institutional arrangements through which financial surpluses are mobilised from the units generating surplus income and transferring them to the others in need of them. The activities include production, distribution, exchange and holding of financial assets/instruments of different kinds by financial institutions, banks and other intermediaries of the market. In a nutshell, financial market, financial assets, financial services and financial institutions constitute the financial system.

Various factors influence the capital market and its growth. These include level of savings in the household sector, taxation levels, health of economy, corporate performance, industrial trends and common patterns of living.

The strength of the economy is calibrated by different economic indicators like growth in GDP (Gross Domestic Product), Agricultural production, quantum and spread of rain fall, interest rates, inflation, position on balance of payments and balance of trade, levels of foreign exchange reserves and investments and growth in capital formation.

The traditional form of financing companies projects consist of internal resources and debt financing, particularly from financial institutions for modernisation, expansion and diversification. The upsurge in performance of certain large companies and the astounding increase of their share prices boost the market sentiment to divert the savings more and more into equity investments in companies. This lead to the growth of equity cult among investors to contribute resources not only for companies but even for financial institutions and banks.

The functions of a good financial system are manifold. They are:

- (a) regulation of currency
- (b) banking functions
- (c) performance of agency services and custody of cash reserves
- (d) management of national reserves of international currency
- (e) credit control
- (f) administering national, fiscal and monetary policy to ensure stability of the economy
- (g) supply and deployment of funds for productive use
- (h) maintaining liquidity.

Long term growth of financial system is ensured through:

- (a) education of investors
- (b) giving autonomy to FIs to become efficient under competition
- (c) consolidation through mergers
- (d) facilitating entry of new institutions to add depth to the market
- (e) minimising regulatory measures and market segmentation.

ORGANISATIONAL STRUCTURE OF FINANCIAL SYSTEM

Broadly, organisational structure of financial system includes various components i.e., Financial Markets, Products and Market Participants.

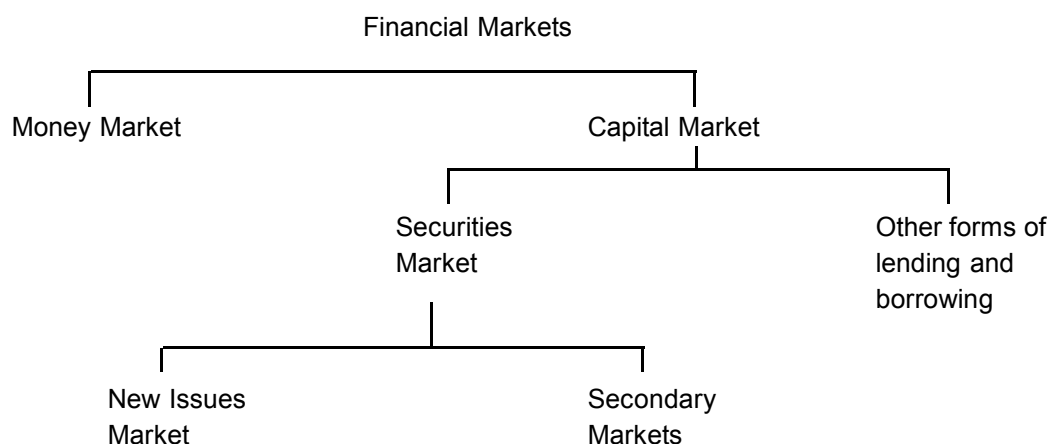
Constituents of Financial System

- Financial Markets
- Products
- Market participants

Financial Markets

Efficient transfer of resources from those having idle resources to others who have a pressing need for them is achieved through financial markets. Stated formally, financial markets provide channels for allocation of savings to investment. These provide a variety of assets to savers as well as various forms in which the investors can raise funds and thereby decouple the acts of saving and investment. The savers and investors are constrained not by their individual abilities, but by the economy's ability, to invest and save respectively. The financial markets, thus, contribute to economic development to the extent that the latter depends on the rates of savings and investment.

The financial markets have two major components; the money market and the capital market.



Money Market

The money market refers to the market where borrowers and lenders exchange short-term funds to solve their liquidity needs. Money market instruments are generally financial claims that have low default risk, maturities under one year and high marketability.

Capital Market

The Capital Market is a market for financial investments that are direct or indirect claims to capital. It is wider than the Securities Market and embraces all forms of lending and borrowing, whether or not evidenced by the creation of a negotiable financial instrument. The Capital Market comprises the complex of institutions and mechanisms through which intermediate term funds and long term funds are pooled and made available to business, government and individuals. The Capital Market also encompasses the process by which securities already outstanding are transferred.

The capital market and in particular the stock exchange is referred to as the barometer of the economy. Government's policy is so moulded that creation of wealth through products and services is facilitated and

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surpluses and profits are channelised into productive uses through capital market operations. Reasonable opportunities and protection are afforded by the Government through special measures in the capital market to get new investments from the public and the Institutions and to ensure their liquidity.

NEED FOR CAPITAL MARKET

Capital market plays an extremely important role in promoting and sustaining the growth of an economy.

- It is an important and efficient conduit to channel and mobilize funds to enterprises, both private and government.
- It provides an effective source of investment in the economy.
- It plays a critical role in mobilizing savings for investment in productive assets, with a view to enhancing a country's long-term growth prospects, and thus acts as a major catalyst in transforming the economy into a more efficient, innovative and competitive marketplace within the global arena.
- In addition to resource allocation, capital markets also provide a medium for risk management by allowing the diversification of risk in the economy.
- A well-functioning capital market tends to improve information quality as it plays a major role in encouraging the adoption of stronger corporate governance principles, thus supporting a trading environment, which is founded on integrity.
- Capital market has played a crucial role in supporting periods of technological progress and economic development throughout history.
- Among other things, liquid markets make it possible to obtain financing for capital-intensive projects with long gestation periods. This certainly held true during the industrial revolution in the 18th century and continues to apply even as we move towards the so-called "New Economy".
- Capital markets make it possible for companies to give shares to their employees via ESOPs.
- Capital markets provide a currency for acquisitions via share swaps.
- Capital markets provide an excellent route for disinvestments to take place.
- Venture Capital and Private Equity funds investing in unlisted companies get an exit option when the company gets listed on the capital markets
- The existence of deep and broad capital market is absolutely crucial in spurring the growth of our country. An essential imperative for India has been to develop its capital market to provide alternative sources of funding for companies and in doing so, achieve more effective mobilisation of investors' savings. Capital market also provides a valuable source of external finance.

For a long time, the Indian market was considered too small to warrant much attention. However, this view has changed rapidly as vast amounts of both international and domestic investment have poured into our markets over the last decade. The Indian market is no longer viewed as a static universe but as a constantly evolving one providing attractive opportunities to the investing community.

FUNCTIONS OF THE CAPITAL MARKET

The major objectives of capital market are:

- To mobilize resources for investments.
- To facilitate buying and selling of securities.
- To facilitate the process of efficient price discovery.

- To facilitate settlement of transactions in accordance with the predetermined time schedules.

Securities Market

The Securities Market, refers to the markets for those financial instruments/claims/obligations that are commonly and readily transferable by sale. The Securities Market has two inter-dependent and inseparable segments, the new issues (primary) market and the stock (secondary) market.

Primary Market

The primary market provides the channel for sale of new securities, while the secondary market deals in securities previously issued. The issuer of securities sells the securities in the primary market to raise funds for investment and/or to discharge some obligation.

In other words, the market wherein resources are mobilised by companies through issue of new securities is called the primary market. These resources are required for new projects as well as for existing projects with a view to expansion, modernisation, diversification and upgradation.

The Primary Market (New Issues) is of great significance to the economy of a country. It is through the primary market that funds flow for productive purposes from investors to entrepreneurs. The latter use the funds for creating new products and rendering services to customers in India and abroad. The strength of the economy of a country is gauged by the activities of the Stock Exchanges. The primary market creates and offers the merchandise for the secondary market.

Secondary Market

The secondary market enables those who hold securities to adjust their holdings in response to changes in their assessment of risk and return. They also sell securities for cash to meet their liquidity needs. The price signals, which subsume all information about the issuer and his business including associated risk generated in the secondary market, help the primary market in allocation of funds.

Secondary market essentially comprises of stock exchanges which provide platform for purchase and sale of securities by investors. The trading platform of stock exchanges are accessible only through brokers and trading of securities is confined only to stock exchanges.

The stock market or secondary market ensures free marketability, negotiability and price discharge. For these reasons the stock market is referred to as the nerve centre of the capital market, reflecting the economic trend as well as the hopes, aspirations and apprehensions of the investors.

This secondary market has further two components, First, the spot market where securities are traded for immediate delivery and payment, The other is futures market where the securities are traded for future delivery and payment. Another variant is the options market where securities are traded for conditional future delivery. Generally, two types of options are traded in the options market. A put option permits the owner to sell a security to the writer of the option at a pre-determined price before a certain date, while a call option permits the buyer to purchase a security from the writer of the option at a particular price before a certain date.

Products and Market Participants

Savings are linked to investments by a variety of intermediaries through a range of complex financial products called “securities” which is defined in the Securities Contracts (Regulation) Act, 1956 to include shares, scrips, stocks, bonds, debentures, debenture stock, or other marketable securities of like nature in or of any incorporate company or body corporate, government securities, derivatives of securities, units of collective investment scheme, security receipts, interest and rights in securities, or any other instruments so declared by the central government. There are a set of economic units who demand securities in lieu of funds and others who supply securities for

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funds. These demand for and supply of securities and funds determine, under competitive market conditions in goods and securities market, the prices of securities.

It is not that the suppliers of funds and suppliers of securities meet each other and exchange funds for securities. It is difficult to accomplish such double coincidence of wants. The amount of funds supplied by the supplier of funds may not be the amount needed by the supplier of securities. Similarly, the risk, liquidity and maturity characteristics of the securities may not match preference of the supplier of funds. In such cases, they incur substantial search costs to find each other. Search costs are minimised by the intermediaries who match and bring these suppliers together. They may act as agents to match the needs of the suppliers of funds / securities, help them in creation and sale of securities or buy the securities issued by supplier of securities and in turn, sell their own securities to suppliers of funds. It is, thus, a misnomer that securities market disintermediates by establishing a direct relationship between the suppliers of funds and suppliers of securities. The market does not work in a vacuum; it requires services of a large variety of intermediaries like merchant bankers, brokers, etc to bring the suppliers of funds and suppliers of securities together for a variety of transactions. The disintermediation in the securities market is in fact an intermediation with a difference; it is a risk-less intermediation, where the ultimate risks are borne by the suppliers of funds/securities (issuers of securities and investors in securities), and not the intermediaries.

The securities market, thus, has essentially three categories of participants, namely the issuers of securities, investors in securities and the intermediaries. The issuers and investors are the consumers of services rendered by the intermediaries while the investors are consumers of securities issued by issuers. Those who receive funds in exchange for securities and those who receive securities in exchange for funds often need the reassurance that it is safe to do so. This reassurance is provided by the law and custom, often enforced by the regulator. The regulator develops fair market practices and regulates the conduct of issuers of securities and the intermediaries so as to protect the interests of investors in securities. The regulator ensures a high standard of service from intermediaries and supply of quality securities and non-manipulated demand for them in the market.

FUNCTIONS OF SECURITIES MARKET

The Securities Market allows people to do more with their savings than they would otherwise could. It also provides financing that enables people to do more with their ideas and talents than would otherwise be possible. The people's savings are matched with the best ideas and talents in the economy. Stated formally, the Securities Market provides a linkage between the savings and the investment across the entities, time and space. It mobilises savings and channelises them through securities into preferred enterprises.

The Securities Market also provides a market place for purchase and sale of securities and thereby ensures transferability of securities, which is the basis for the joint stock enterprise system. The existence of the Securities Market makes it possible to satisfy simultaneously the needs of the enterprises for capital and the need of investors for liquidity.

Takeaways

Securities Market –

- *Is a link between investment & savings*
- *Mobilises & channelises savings*
- *Provides Liquidity to investors*
- *Is a market place for purchase and sale of securities*

The liquidity, the market confers and the yield promised or anticipated on security ownership may be sufficiently

great to attract net savings of income which would otherwise have been consumed. Net savings may also occur because of other attractive features of security ownership, e.g. the possibility of capital gain or protection of savings against inflation.

A developed Securities Market enables all individuals, no matter how limited their means, to share the increased wealth provided by competitive private enterprises. The Securities Market allows individuals who can not carry an activity in its entirety within their resources to invest whatever is individually possible and preferred in that activity carried on by an enterprise. Conversely, individuals who can not begin an enterprise, they can attract enough investment from others to make a start. In both cases individuals who contribute to the investment made in the enterprise share the fruits. The Securities Market, by allowing an individual to diversify risk among many ventures to offset gains and losses, increases the likelihood of long-term, overall success.

SECURITIES MARKET AND ECONOMIC GROWTH

A well functioning securities market is conducive to sustained economic growth. There have been a number of studies, starting from World Bank and IMF to various scholars, which have established robust relationship not only one way, but also the both ways, between the development in the securities market and the economic growth. The securities market fosters economic growth to the extent that it-(a) augments the quantities of real savings and capital formation from any given level of national income, (b) increases net capital inflow from abroad, (c) raises the productivity of investment by improving allocation of investible funds, and (d) reduces the cost of capital.

It is reasonable to expect savings and capital accumulation and formation to respond favourably to developments in securities market. The provision of even simple securities decouples individual acts of saving from those of investment over both time and space and thus allows savings to occur without the need for a concomitant act of investment. If economic units rely entirely on self-finance, investment is constrained in two ways: by the ability and willingness of any unit to save, and by its ability and willingness to invest. The unequal distribution of entrepreneurial talents and risk taking proclivities in any economy means that at one extreme there are some whose investment plans may be frustrated for want of enough savings, while at the other end, there are those who do not need to consume all their incomes but who are too inert to save or too cautious to invest the surplus productively. For the economy as a whole, productive investment may thus fall short of its potential level. In these circumstances, the securities market provides a bridge between ultimate savers and ultimate investors and creates the opportunity to put the savings of the cautious at the disposal of the enterprising, thus promising to raise the total level of investment and hence of growth. The indivisibility or lumpiness of many potentially profitable but large investments reinforces this argument. These are commonly beyond the financing capacity of any single economic unit but may be supported if the investor can gather and combine the savings of many. Moreover, the availability of yield bearing securities makes present consumption more expensive relative to future consumption and, therefore, people might be induced to consume less today. The composition of savings may also change with fewer saving being held in the form of idle money or unproductive durable assets, simply because more divisible and liquid assets are available.

International Linkage

The securities market facilitates the internationalisation of an economy by linking it with the rest of the world. This linkage assists through the inflow of capital in the form of portfolio investment. Moreover, a strong domestic stock market performance forms the basis for well performing domestic corporate to raise capital in the international market. This implies that the domestic economy is opened up to international competitive pressures, which help to raise efficiency. It is also very likely that existence of a domestic securities market will deter capital outflow by providing attractive investment opportunities within domestic economy.

Improved Investment Allocation

Any financial development produces allocational improvement over a system of segregated investment opportunities. The benefits of improved investment allocation is such that Mc Kinnon defines economic development as reduction of the great dispersion in social rate of return to existing and new investments under domestic entrepreneurial control. Instead of emphasising scarcity of capital, he focuses on the extra-ordinary distortions commonly found in the domestic securities markets of the developing countries. In the face of great discrepancies in rate of return, the accumulation of capital does not contribute much to development. A developed securities market successfully monitors the efficiency with which the existing capital stock is deployed.

Standardised products and reduction in costs

In as much as the securities market enlarges the financial sector, promoting additional and more sophisticated financing, it increases opportunities for specialisation, division of labour and reductions in costs in financial activities. The securities market and its institutions help the user in many ways to reduce the cost of capital. They provide a convenient market place to which investors and issuers of securities go and thereby avoid the need to search a suitable counterpart. The market provides standardised products and thereby cuts the information costs associated with individual instruments. The market institutions specialise and operate on large scale which cuts costs through the use of tested procedures and routines.

Developmental benefits

There are also other developmental benefits associated with the existence of a securities market;

1. The securities market provides a fast-rate breeding ground for the skills and judgement needed for entrepreneurship, risk bearing, portfolio selection and management.
2. An active securities market serves as an 'engine' of general financial development and may, in particular, accelerate the integration of informal financial systems with the institutional financial sector. Securities directly displace traditional assets such as gold and stocks of produce or indirectly, may provide portfolio assets for unit trusts, pension funds and similar FIs that raise savings from the traditional sector.
3. The existence of securities market enhances the scope and provides institutional mechanisms, for the operation of monetary and financial policy.

PROFILE OF SECURITIES MARKET

Public and Rights Issues¹

Resource mobilisation through primary market, in terms of amount raised, slightly moderated during July 2017 compared to the previous month. Nevertheless, the number of issues remained the same. During the month under review, the primary market witnessed 15 issues that mobilised Rs. 2,838 crore compared to 15 issues during June 2017 that mobilised Rs. 5,632 crore. There were 14 public issues that raised Rs. 2,639 crore during July 2017. Out of the 14 public issues made during July 2017, there were 12 equity IPOs raising Rs. 909 crore and two debt issues that raised Rs. 1,730 crore. There was one rights issue that raised Rs. 199 crore.

QIPs Listed at BSE and NSE

QIP is an alternative mode of resource raising available for listed companies to raise funds from domestic market. In a QIP, a listed issuer issues equity shares or non-convertible debt instruments along with warrants and convertible securities other than warrants to Qualified Institutions Buyers only.

There were four QIP issues during July 2017 which raised Rs.2, 775 crore compared to Rs. 15,000 crore raised through one QIP issue in the previous month.

¹ Source: SEBI Bulletin , Edition August, 2017

Preferential Allotments Listed at BSE and NSE

Preferential allotment also serves as an alternative mechanism of resource mobilization wherein a listed issuer issues shares or convertible securities, to a select group of persons. There were 28 preferential allotments (Rs. 561 crore) listed at BSE and NSE during July 2017, compared to 40 preferential allotments (amounting to Rs. 4,825 crore) listed during June, 2017.

Resource Mobilisation by Mutual Funds

During July 2017, there was a net inflow of Rs. 63,505 crore into the mutual funds industry against a net outflow of Rs. 16,593 crore during June 2017. In the month under review, there were inflow of Rs. 41,223 crore from income / debt oriented schemes whereas inflow of Rs. 12,728 crore into growth / equity oriented schemes. Balanced schemes recorded inflow of Rs. 7,864 crore. The Fund of funds schemes investing overseas recorded net outflow of Rs. 26 crore. The cumulative net assets under management by all mutual funds rose by 5.1 per cent to Rs. 19,96,905 crore at the end of July 2017 from Rs. 18,96,291 crore at the end of June 2017.

Depository Accounts

The total number of investor accounts was 160 lakh at NSDL and 130 lakh at CDSL at the end of July 2017. In July 2017, the number of investor accounts at NSDL and CDSL increased by 8 percent and 15.4 percent, respectively.

Investment by Mutual Funds

The total net investment in the secondary market by mutual funds was Rs. 52,187 crore in July 2017 out of which Rs. 11,800 crore was invested in equity and Rs. 40,388 crore was invested in debt. This is an increase over total investment of Rs. 21,724 crore in June 2017 out of which Rs. 9,106 crore was invested in equity and Rs. 12,618 crore was invested in debt.

As on July 31, 2017, there were a total of 2,041 mutual fund schemes in the market, of which 1,423 (69.7 per cent) were income / debt oriented schemes, 493 (24.2 per cent) were growth / equity oriented schemes, 31 (1.5 per cent) were balanced schemes, 65 (3.2 per cent) were exchange traded funds and 29 (1.4 per cent) were fund of funds investing overseas.

Investment by Foreign Portfolio Investors (FPIs)

In June 2017, the FPIs remained net buyers in the Indian securities market to the tune of Rs. 24,028 crore. There were net inflow of Rs. 5,161 crore in equity and Rs. 18,867 crore in debt.

The assets of the FPIs in India, as reported by the custodians, at the end of July 2017 was Rs. 30,55,984 crore, out of which the notional value of offshore derivative instruments (including ODIs on derivatives) was Rs. 1,35,297 crore, constituting 4.4 per cent of the total assets under custody of FPIs.

MARKET REGULATION

It is important to ensure smooth working of capital market, as it is the arena for the players associated with the economic growth of the country. Various laws have been passed from time to time to meet this objective. The financial market in India was highly segmented until the initiation of reforms in 1992-93 on account of a variety of regulations and administered prices including barriers to entry. The reform process was initiated with the establishment of Securities and Exchange Board of India.

The main legislations governing the Capital Market are:—

1. The SEBI Act, 1992 which establishes SEBI to protect investors and develop and regulate securities market.
2. The Securities Contracts (Regulation) Act, 1956, SC(R) Act which regulates transactions in securities through control over stock exchanges.

3. The Depositories Act, 1996 which provides for electronic maintenance and transfer of ownership of demat securities.
4. The Companies Act, 2013, which sets out the code of conduct for the corporate sector in relation to issue, allotment and transfer of securities and disclosures to be made in public issues.

SEBI ACT, 1992

The SEBI Act, 1992 establishes SEBI with statutory powers for (a) protecting the interests of investors in securities, (b) promoting the development of the securities market, and (c) regulating the securities market. Its regulatory jurisdiction extends over corporates in the issuance of capital and transfer of securities, in addition to all intermediaries and persons associated with securities market. It can conduct enquiries, audits and inspection of all concerned and adjudicate offences under the Act. It has powers to register and regulate all market intermediaries and also to penalise them in case of violations of the provisions of the Act, Rules and Regulations made there under. SEBI has full autonomy and authority to regulate and develop an orderly securities market.

SECURITIES CONTRACTS (REGULATION) ACT, 1956

It provides for direct and indirect control of virtually all aspects of securities trading and the running of stock exchanges and aims to prevent undesirable transactions in securities. It gives central government/SEBI regulatory jurisdiction over (a) stock exchanges through a process of recognition and continued supervision, (b) contracts in securities, and (c) listing of securities on stock exchanges. As a condition of recognition, a stock exchange complies with prescribed conditions of Central Government. Organised trading activity in securities takes place on a specified recognised stock exchange. The stock exchanges determine their own listing regulations which have to conform to the minimum listing criteria set out in the Rules.

DEPOSITORIES ACT, 1996

The Depositories Act, 1996 provides for the establishment of depositories in securities with the objective of ensuring free transferability of securities with speed, accuracy and security by (a) making securities of public limited companies freely transferable subject to certain exceptions; (b) dematerializing the securities in the depository mode; and (c) providing for maintenance of ownership records in a book entry form. In order to streamline the settlement process, the Act envisages transfer of ownership of securities electronically by book entry without making the securities move from person to person. The Act has made the securities of all public limited companies freely transferable, restricting the company's right to use discretion in effecting the transfer of securities, and the transfer deed and other procedural requirements under the Companies Act have been dispensed with.

COMPANIES ACT, 2013

The Companies Act, 2013 has replaced the Companies Act, 1956. The Companies Act, 2013 envisage to strengthen the existing regulatory framework on Corporate Governance. It deals with issue, allotment and transfer of securities and various aspects relating to company management. It provides for standard of disclosure in public issues of capital, particularly in the fields of company management and projects, information about other listed companies under the same management, and management perception of risk factors. It also regulates underwriting, the use of premium and discounts on issues, rights and bonus issues, payment of interest and dividends, supply of annual report and other information.

SECURITIES MARKET REFORMS & REGULATORY MEASURES TO PROMOTE INVESTOR CONFIDENCE

SEBI has come a long way since its inception as an institution regulating the Indian Capital Markets. It has initiated a lot of reforms to make the market more safer for investors. The following are the major policy initiatives taken by SEBI since its inception.

- **Control over Issue of Capital:** A major initiative of liberalisation was the repeal of the Capital Issues (Control) Act, 1947 in May 1992. In the interest of investors, SEBI issued Disclosure and Investor Protection (DIP) guidelines. The guidelines allow issuers, complying with the eligibility criteria, to issue securities the securities at market determined rates. The market moved from merit based to disclosure based regulation.
- **Establishment of Regulator:** A major initiative of regulation was, establishment of a statutory autonomous agency, called SEBI, to provide reassurance that it is safe to undertake transactions in securities.
- **Screen Based Trading:** A major developmental initiative was a nation-wide on-line fully-automated screen based trading system (SBTS) where a member can punch into the computer quantities of securities 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 counter party.
- **Risk management:** A number of measures were taken to manage the risks in the market so that the participants are safe and market integrity is protected. The trading cycle varied from 14 days for specified securities to 30 days for others and settlement took another fortnight. Rolling settlement on T+5 basis was introduced in phases. All scrips moved to rolling settlement from December 2001. T+5 gave way to T+3 from April 2002 and T+2 from April 2003.
- **Depositories Act:** The earlier settlement system gave rise to settlement risk. This was due to the time taken for settlement and due to the physical movement of paper. Further, the transfer of shares in favour of the purchaser by the company also consumed considerable amount of time. To obviate these problems, the Depositories Act, 1996 was passed to provide for the establishment of depositories in securities.
- **Derivatives:** To assist market participants to manage risks better through hedging, speculation and arbitrage, SC(R)A was amended in 1995 to lift the ban on options in securities.
- **Settlement Guarantee:** A variety of measures were taken to address the risk in the market. Clearing corporations emerged to assume counter party risk. Trade and settlement guarantee funds were set up to guarantee settlement of trades irrespective of default by brokers. These funds provide full novation and work as central counter party. The Exchanges /clearing corporations monitor the positions of the brokers on real time basis. The securities market moved from T+3 settlement period to T+2 rolling settlement with effect from April 1, 2003. Further, straight through processing has been made mandatory for all institutional trades executed on the stock exchange.
- **Securities Market Awareness:** In January 2003, SEBI launched a nation-wide Securities Market Awareness Campaign that aims at educating investors about the risks associated with the market as well as the rights and obligations of investors.
- **Green Shoe Option-** As a stabilization tool for post listing price of newly issued shares, SEBI has introduced the green shoe option facility in IPOs.
- **Securities Lending and Borrowing-** A clearing corporation/clearing house, after registration with SEBI, under the SEBI scheme for Securities Lending and Borrowing, as an approved intermediary, may borrow securities for meeting shortfalls in settlement, on behalf of the members.
- **Corporate Governance -** To improve the standards of corporate governance, SEBI amended Clause 49 of the Listing Agreement. The major changes in the new Clause 49 include amendments/additions to provisions relating to definition of independent directors, strengthening the responsibilities of audit committees, improving quality of financial disclosures, including those pertaining to related party transactions and proceeds from public/rights/preferential issues, requiring Boards to adopt formal code of conduct, requiring CEO/CFO certification of financial statements and improving disclosures to

shareholders. Certain non-mandatory clauses like whistle blower policy and restriction of the term of independent directors have also been included.

- **Debt Listing Agreement-** In order to further develop the corporate debt market, SEBI prescribed a model debenture listing agreement for all debenture securities issued by an issuer irrespective of the mode of issuance.
- **Gold Exchange Traded Funds in India-** Pursuant to the announcement made by the Honourable Finance Minister in his Budget Speech for 2005-06, SEBI appointed a Committee for the introduction of Gold Exchange Traded Fund (GETF) in India. Based on the recommendations of the said Committee, the SEBI (Mutual Funds) Regulations, 1996 were amended and notification was issued on January 12, 2006 permitting mutual funds to introduce GETFs in India subject to certain investment restrictions.
- **Guidelines for Issue of Indian Depository Receipts (IDRs)-** SEBI issued Guidelines on disclosures and related requirements for companies desirous of issuing IDRs in India. SEBI also prescribed the listing agreement for entities issuing IDRs.
- **Grading of Initial Public offerings (IPOs)-** Grading of all IPOs was made mandatory. The grading would be done by credit rating agencies, registered with SEBI. It would be mandatory to obtain grading from at least one credit rating agency. The grading would be disclosed in the prospectus, abridged prospectus and in every advertisement for IPOs.
- **Introduction of Fast Track Issuances-** To enable compliant listed companies to access Indian primary market in a time effective manner through follow-on public offerings and rights issues, SEBI introduced fast track issue mechanism. To make the issuance process fast, the earlier requirement of filing draft offer documents was amended and the need to file draft offer documents with SEBI and the stock exchanges was done away with.
- **Mandatory Requirement of Permanent Account Number (PAN) for All Transactions in the Securities Market-** SEBI stipulated that PAN would be the sole identification number for all participants in the securities market, irrespective of the amount of transaction with effect from July 02, 2007. The objective was to strengthen the 'Know Your Client' (KYC) norms through a single identification number for all participants in the securities market for facilitating sound audit trail.
- **Corporate Debt Market-** In order to develop a sound corporate debt market in India, SEBI took a number of policy initiatives with respect to the following areas: (i) setting up of reporting platforms for corporate bonds, (ii) setting up of trading platform for corporate bonds, (iii) issues pertaining to trading in corporate bonds, (iv) making amendments to the listing agreement for debentures, (v) issuing securitised debt instruments regulations, (vi) evolving policy guidelines on debenture trustees, (vii) introducing Repos in corporate bonds, (viii) facilitating setting up of quote dissemination platforms, (ix) simplifying corporate bond issuance norms and (x) framing of draft issue and listing regulations for corporate bonds.
- **Setting up of SME Exchange-** SEBI decided to put in place a framework for setting up of new exchange or separate platform of existing stock exchange having nationwide terminals for SME. In order to operationalise the said framework, necessary changes have been made to applicable regulations, circulars etc. As per the framework, market making has been made mandatory in respect of all scrips listed and traded on SME exchange.
- SEBI made ASBA bid-cum application forms available for download and printing, from websites of the Stock Exchanges which provide electronic interface for ASBA facility i.e. Bombay Stock Exchange (BSE) and National Stock Exchange (NSE). The ASBA forms so downloaded should have a unique application number and can be used for making ASBA applications in public issues.

- In order to develop the primary market for securitized debt instruments in India, SEBI notified the Securities and Exchange Board of India (Public offer and Listing of Securitised Debt Instruments) Regulations, 2008. The regulations provide for a framework for issuance and listing of securitized debt instruments by a Special Purpose Distinct Entity (SPDE).
- SEBI has commenced processing of investor grievances against the intermediaries in a centralized web-based complaints redressal system, 'SCORES' at <http://scores.gov.in/Admin>.
- Facility of e-voting by shareholders enabled on July 13, 2012.
- **Business Responsibility Reports**- SEBI inserted Clause 55 in the Equity Listing Agreement, mandating inclusion of Business Responsibility Reports ("BR reports") as part of the Annual Reports for listed entities in line with the 'National Voluntary Guidelines on Social, Environmental and Economic Responsibilities of Business' issued by the Ministry of Corporate Affairs.
- SEBI notified the SEBI (Foreign Portfolio Investors) Regulations 2014 (FPI Regulations) on January 07, 2014 to simplify compliance requirements and have uniform guidelines for various categories of Foreign Portfolio Investors (FPIs) like Foreign Institutional Investors (FIIs) including their sub-accounts, if any and Qualified Foreign Investors (QFIs).
- SEBI (Real Estate Investment Trusts) Regulations, 2014 and SEBI (Infrastructure Investment Trusts) Regulations, 2014 were notified on 26 September, 2014.
- SEBI (Share Based Employee Benefits) Regulations, 2014 were notified.
- Consolidated circular was issued on redressal of investor grievances through SCORES platform.
- SEBI (Depositories and Participants) Regulations were amended providing single and permanent registration of DP through any depository.
- SEBI revised the mechanism of index based market-wide circuit breaker.
- On basis of recommendation of Depository Systems Review Committee, SEBI issued risk management policy framework for the Depositories.
- SEBI (Prohibition of Insider Trading) Regulations, 2015 were notified.
- With a view to increase participation, resident individual investors were allowed to open a trading account and demat account by filling up a simplified Saral Account Opening Form.
- Amendments were carried out to the provisions of SEBI (ICDR) Regulations, 2009 in respect of investment in partly paid shares and warrants.
- SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (Listing Regulations) were notified on 02 September, 2015.
- Shri Arun Jaitley, Hon'ble Union Finance Minister, unveiled the historic merger of Forward Markets Commission (FMC) with SEBI at an event in Mumbai, on September 28, 2015.
- **Empowerment of Stock Exchanges for Effective Regulation of Listed Entities** : In order to empower the stock exchanges for effective regulations of listed entities, amendments have been notified to the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009 (ICDR Regulations) to enable actions such as imposition of fines and suspension of trading by stock exchanges for contravention of ICDR Regulations.
- **Extension of the Applicability of Business Responsibility Reporting Requirements** : The applicability of BRR requirements has now been extended to the top 500 listed entities based on market capitalization as on March 31 of every year. Further, as a green initiative, BRRs are permitted to be made available on the websites of the companies with links to the websites being made available in their annual reports.

- **Streamlining the Process of System-driven Disclosures:** SEBI has put in place a framework for system driven disclosures wherein the onus of disclosures has been shifted from individuals/companies to the securities market infrastructure through an integration among depositories, stock exchanges and the registrar and transfer agents (RTAs). Such a system will help in eliminating the possibility of inadvertent violations by the entities and will also help in providing information to investors on a timely basis to take investment decisions thus leading to fairness in the markets.
- **Transparency in Listed Companies Dividend Distribution Policies:** In order to bring in more transparency with respect to listed companies dividend policies, a new Regulation 43A has been introduced in the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015. This requires the top 500 listed companies (by way of market capitalization) to formulate and disclose their dividend distribution policies in their annual reports and on their websites.
- **Enhanced Corporate Governance Standards:** To address concerns related to private equity funds entering into compensation agreements to incentivize promoters, directors and key managerial personnel of listed investee companies which could potentially lead to unfair practices, the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2016 (Listing Regulations) were amended to put in place provisions for disclosures and approval of the board and shareholders.
- **Enhancing the Ceiling on Employee Reservation in Issues:** As per SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009, an issuer can make reservation for employees not exceeding 5 per cent of the post issue capital of the issuer. The value of allotment to any employee in pursuance of reservation was restricted to Rs. 2 lakh. SEBI has now allowed allotment to employees in excess of the extant limit of Rs. 2 lakh per employee under the employee reservation quota. The value of total allotment to an employee under the employee reservation portion, including the additional allotment shall not exceed Rs. 5 lakh.

The details regarding various initiatives of SEBI are covered separately at respective in the Study Material.

FEATURES OF DEVELOPED CAPITAL MARKET: THE INTERNATIONAL ORGANIZATION OF SECURITIES COMMISSIONS (IOSCO)

BACKGROUND

The International Organization of Securities Commissions (IOSCO) was created in 1983 with the decision to change from an inter-American regional association (created in 1974) into a global cooperative body. Eleven securities regulatory agencies from North and South America took this decision in April 1983 at a meeting in Quito, Ecuador.

In 1984, securities regulators from France, Indonesia, Korea and the United Kingdom were the first agencies to join the organization from outside the Americas. The IOSCO Annual Conference in July 1986, held in Paris, was the first to take place outside of the western hemisphere. It was decided at this meeting to create a permanent General Secretariat for IOSCO.

Today IOSCO is recognized as the international standard setter for securities markets. Its membership regulates more than 95% of the world's securities markets and it is the primary international cooperative forum for securities market regulatory agencies. IOSCO members are drawn from, and regulate, over 100 jurisdictions and its membership continues to grow.

IOSCO provides comprehensive technical assistance to its members, in particular those which regulate emerging securities markets.

In 1998, IOSCO adopted a comprehensive set of Objectives and Principles of Securities Regulation (IOSCO Principles), which is recognized as the international regulatory benchmarks for all securities markets. In 2003,

the organization endorsed a comprehensive methodology (IOSCO Principles Assessment Methodology) that enables an objective assessment of the level of implementation of the IOSCO Principles in the jurisdictions of its members and the development of practical action plans to correct identified deficiencies.

In 2002, IOSCO adopted a multilateral memorandum of understanding (IOSCO MMoU) designed to facilitate cross-border enforcement and exchange of information among international securities regulators.

Then in 2005, IOSCO endorsed the IOSCO MMoU as the benchmark for international cooperation among securities regulators and set-out clear strategic objectives to expand the network of IOSCO MMoU signatories by 2010. It approved as an operational priority the effective implementation - in particular within its membership - of the IOSCO Principles and of the IOSCO MMoU, which are considered primary instruments in facilitating cross-border cooperation, reducing global systemic risk, protecting investors and ensuring fair and efficient securities markets. **The Securities and Exchange Board of India is also a signatory to IOSCO MMoU.**

IOSCO OBJECTIVE OF SECURITIES REGULATION

There are three objectives of securities regulation –

- (i) protecting investors;
- (ii) ensuring that markets are fair, efficient and transparent;
- (iii) reducing systemic risk

MEMBERSHIP

CATEGORIES

There are three categories of membership within IOSCO which are designed to the different approaches to securities markets regulation while also ensuring that those with an interest in the regulation of securities markets are also involved in the debate on securities market issues.

The three categories are:

- Ordinary;
- Associate; and
- Affiliate.

ORDINARY

This category is open to a securities commission, or a similar government or statutory regulatory body that has primary responsibility for securities regulation in its jurisdiction.

If there is no governmental, or statutory, regulatory body in a jurisdiction then a self-regulatory body, such as a stock exchange, in that jurisdiction is eligible for ordinary membership of IOSCO. However, the ordinary membership of a self-regulatory body admitted to IOSCO will lapse if a governmental regulatory body from the same jurisdiction becomes the ordinary member for that jurisdiction.

Ordinary members each have one vote in the Presidents Committee, which meets yearly at the Annual Conference.

ASSOCIATE

The following bodies can apply to become associate members of the organization:

1. a public regulatory body with jurisdiction in the subdivisions of a jurisdiction if the national regulatory body is already an ordinary member; and

2. any other eligible body with an appropriate responsibility for securities regulation.

A self regulatory body is not eligible for associate membership.

Associate members do not have the right to vote and are also precluded from membership of the IOSCO Board; however they are members of the Presidents Committee.

AFFILIATE

A self-regulatory body (SRO), or an international body, with an appropriate interest in securities regulation is eligible for this category of membership.

Affiliate members do not have a vote, are not eligible for the IOSCO Board and are not members of the Presidents Committee. SROs affiliate members form the SRO Consultative Committee.

MULTILATERAL MEMORANDUM OF UNDERSTANDING CONCERNING CONSULTATION AND CO-OPERATION AND EXCHANGE OF INFORMATION (MMoU)

The MMoU sets an international benchmark for cross-border co-operation critical to combating violations of securities and derivatives laws.

What is it?

The MMoU represents a common understanding amongst its signatories about how they will consult, cooperate, and exchange information for securities regulatory enforcement purposes.

The MMoU itself sets out the specific requirements for what information can be exchanged and how it is to be exchanged: legal ability to compel information; types of information that can be compelled; legal ability to share information; and permissible uses of information.

It also sets out specific requirements regarding the confidentiality of the information exchanged, and ensures that no domestic banking secrecy, blocking laws or regulations prevents securities regulators from sharing this information with their counterparts in other jurisdictions.

OVER VIEW OF DEPOSITORY SYSTEM IN INDIA

A depository is an organisation which holds securities (like shares, debentures, bonds, government securities, mutual fund units etc.) of investors in electronic form at the request of the investors through a registered Depository Participant. India has adopted the Depository System for securities trading in which book entry is done electronically and no paper is involved. The physical form of securities is extinguished and shares or securities are held in an electronic form.

KEY FEATURES OF THE DEPOSITORY SYSTEM IN INDIA

1. Multi-Depository System: The depository model adopted in India provides for a competitive multi-depository system. There can be various entities providing depository services. A depository should be a company formed under the Companies Act, 2013 (erstwhile Companies Act, 1956) and should have been granted a certificate of registration under the Securities and Exchange Board of India Act, 1992. Presently, there are two depositories registered with SEBI, namely:

- National Securities Depository Limited (NSDL), and
- Central Depository Service Limited (CDSL)

2. Depository services through depository participants: The depositories can provide their services to investors through their agents called depository participants. These agents are appointed subject to the conditions prescribed under Securities and Exchange Board of India (Depositories and Participants) Regulations, 1996 and other applicable conditions.

3. Dematerialisation: The model adopted in India provides for dematerialisation of securities. This is a significant step in the direction of achieving a completely paper-free securities market. Dematerialization is a process by which physical certificates of an investor are converted into electronic form and credited to the account of the depository participant.

4. Fungibility: The securities held in dematerialized form do not bear any notable feature like distinctive number, folio number or certificate number. Once shares get dematerialized, they lose their identity in terms of share certificate, distinctive numbers and folio numbers. Thus all securities in the same class are identical and interchangeable. For example, all equity shares in the class of fully paid up shares are interchangeable.

5. Registered Owner/ Beneficial Owner: In the depository system, the ownership of securities dematerialized is bifurcated between Registered Owner and Beneficial Owner. According to the Depositories Act, 1996 'Registered Owner' means a depository whose name is entered as such in the register of the issuer. A 'Beneficial Owner' means a person whose name is recorded as such with the depository. Though the securities are registered in the name of the depository actually holding them, the rights, benefits and liabilities in respect of the securities held by the depository remain with the beneficial owner. For the securities dematerialized, NSDL/CDSL is the Registered Owner in the books of the issuer; but ownership rights and liabilities rest with Beneficial Owner. All the rights, duties and liabilities underlying the security are on the beneficial owner of the security.

6. Free Transferability of shares: Transfer of shares held in dematerialized form takes place freely through electronic book-entry system.

LESSON ROUND UP

- The Securities Market refers to the markets for those financial instruments/ claims/obligations that are commonly and readily transferable by sale.
- The Securities Market has two inter-dependent and inseparable segments, the new issues (primary) market and the stock (secondary) market.
- The primary market provides the channel for sale of new securities, while the secondary market deals in securities previously issued.
- The four main legislations governing the securities market are: the SEBI Act, 1992; the Companies Act, 2013; the Securities Contracts (Regulation) Act, 1956 and the Depositories Act, 1996.
- Today IOSCO is recognized as the international standard setter for securities markets. Its membership regulates more than 95% of the world's securities markets and it is the primary international cooperative forum for securities market regulatory agencies.
- India has adopted the Depository System for securities trading in which book entry is done electronically and no paper is involved.

GLOSSARY

Boom	A condition of the market denoting increased activity with rising prices and higher volume of business resulting from greater demand of securities. It is a state where enlarged business, both investment and speculative, has been taking place for a sufficiently reasonable period of time.
Corporate Governance	The way in which companies run themselves, in particular the way in which they are accountable to those who have a vested interest in their performance, especially their shareholders.

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation.)

- [illegible]

Lesson 2

Capital Market Instruments

LESSON OUTLINE

- Introduction
- Classification of Instruments
- Equity Shares
- Shares with Differential Voting Rights
- Preference Shares
- Debentures
- Sweat Equity Shares
- Secured Premium Notes
- Equity Shares with detachable warrants
- Dual Option Warrants
- Debt Instruments with Debt Warrants
- Debt for Equity Swap
- Different types of Bonds & Notes
- Global Depository Receipts
- Foreign Currency Convertible Bonds
- Indian Depository Receipts
- Tracking Stocks
- Mortgage Backed Securities
- Futures
- Options
- Hedge Funds
- Exchange Traded Funds
- Fund of Funds
- LESSON ROUND UP
- GLOSSARY
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

Financial instruments innovation has been a continuous and integral part of growth of the capital markets. A variety of factors such as fluctuation in interest rate, volatility in price, change in tax structures and regulatory changes etc. plays an important part in financial innovation.

In finance, innovation involves adapting and improvising on existing products and concepts. Advances emerge initially as either products (such as derivatives, high-yield corporate bonds, and mortgage-backed securities) or processes (such as pricing mechanisms, trading platforms, and means and methods for distributing securities). By moving funds or enabling investors to pool funds, these tools increase liquidity to facilitate the sale and purchase of goods or the management of risks in markets and enterprises.

In general, it refers to the creating and marketing of new types of securities by the issuers for raising funds from the investor. A financial instrument is a combination of characteristics such as promised yield, liquidity, maturity period, security and risk.

Keeping this in view this lesson is designed to enable the students to understand the various instruments available in the capital market, their features and classification etc.

INTRODUCTION

Financial Instruments that are used for raising capital resources in the capital market are known as capital market instruments. The capital market instruments are usually used by the Government, Corporations and Companies. The instruments used by the corporate sector to raise funds are selected on the basis of – (i) investor preference for a given instrument, (ii) the regulatory framework, which regulate the issue of security.

Factors effecting the preferences for choosing any instruments :

For issuers	For investor
Cost	Return
Post Tax Cost of Capital	Tax on return received
Servicing	Yield
Debt-equity ratio and debt service capabilities	Risk reward ratio
Ceding the control in case of equity	Gaining the control in case of equity
Company Law, SEBI Regulations etc	Marketable and liquidity

CLASSIFICATION OF INSTRUMENTS

Hybrid Instruments

Hybrid instruments are those which are created by combining the features of equity with bond, preference and equity etc. Examples of Hybrid instruments are: Convertible preference shares, Cumulative convertible preference shares, convertible debentures, non convertible debentures with equity warrants, partly convertible debentures, partly convertible debentures with Khokha (buy-back arrangement), Optionally convertible debenture, warrants convertible into debentures or shares, secured premium notes with warrants etc.

Pure Instruments

Equity shares, preference shares and debentures/ bonds which were issued with their basic characteristics intact without mixing features of other classes of instruments are called Pure instruments.

Derivatives Instruments

Derivatives are contracts which derive their values from the value of one or more of other assets (known as underlying assets). The derivative itself is merely a contract between two or more parties. Its value is determined by fluctuations in the underlying asset. The most common underlying assets include stocks, bonds, commodities, currencies, interest rates and market indexes. Some of the most commonly traded derivatives are futures, forward, options and swaps.

EQUITY SHARES

Equity shares, commonly referred to as ordinary share also represents the form of fractional ownership in which a shareholder, as a fractional owner, undertakes the maximum entrepreneurial risk associated with a business venture. The holder of such shares is the member of the company and has voting rights.

According to explanation (i) to Section 43 of Companies Act, 2013 “equity share capital”, with reference to any company limited by shares, means all share capital which is not preference share capital. Section 43 further provides for equity share capital (i) with voting rights, or (ii) with differential rights as to dividend, voting or otherwise in accordance with such rules as may be prescribed.

Equity capital and further issues of equity capital by a company are generally based on the condition that they will rank *pari passu* along with the earlier issued share capital in all respects. However, as regards dividend declared by the company such additional capital shall be entitled to dividend ratably for the period commencing from the date of issue to the last day of the accounting year, unless otherwise specified in the articles or in the terms of the issue.

Important characteristics of equity shares are given below :

Equity shares, have voting rights at all general meetings of the company. These votes have the affect of the controlling the management of the company.

Equity shares have the right to share the profits of the company in the form of dividend (cash) and bonus shares.

However even equity shareholders cannot demand declaration of dividend by the company which is left to the discretion of the Board of Directors.

When the company is wound up, payment towards the equity share capital will be made to the respective shareholders only after payment of the claims of all the creditors and the preference share capital.

Equity share holders enjoy different rights as members under the Companies Act, 2013 such as:

- (a) The right to vote on every resolution placed before the company – (Section 47)
- (b) The rights to subscribe to shares at the time of further issue of capital by the company (Preemptive Right) – (Section 62)
- (c) Right to appoint proxy to attend and vote at the meeting on his behalf – (Section 105)
- (d) Right to receive copy of annual accounts of the company – (Section 136)
- (e) Right to receive notice of the meeting of members – (Section 101)
- (f) Right to inspection of various statutory registers maintained by the company – (Section 94)
- (g) Right to requisition extraordinary general meeting of the company – (Section 100)

SHARES WITH DIFFERENTIAL VOTING RIGHTS

Section 43(a)(ii) of the Companies Act, 2013, authorized equity share capital with differential rights as to dividend, voting or otherwise in accordance with rule 4 of Companies (Share Capital and Debentures) Rules, 2014 which prescribes the following conditions for issue of DVRs :

- (a) the articles of association of the company authorizes the issue of shares with differential rights;
- (b) the issue of shares is authorized by ordinary resolution passed at a general meeting of the shareholders. Where the equity shares of a company are listed on a recognized stock exchange, the issue of such shares shall be approved by the shareholders through postal ballot at a general meeting;
- (c) the shares with differential rights shall not exceed twenty-six percent of the total post-issue paid up equity share capital including equity shares with differential rights issued at any point of time;
- (d) the company having consistent track record of distributable profit for the last three years;
- (e) the company has not defaulted in filing financial statements and annual returns for three financial years immediately preceding the financial year in which it is decided to issue such shares;
- (f) the company has no subsisting default in the payment of a declared dividend to its shareholders or repayment of its matured deposits or redemption of its preference shares or debentures that have become due for redemption or payment of interest on such deposits or debentures or payment of dividend;

- (g) the company has not defaulted in payment of the dividend on preference shares or repayment of any term loan from a public financial institution or state level financial institution or scheduled bank that has become repayable or interest payable thereon or dues with respect to statutory payments relating to its employees to any authority or default in crediting the amount in Investor Education and Protection Fund to the Central Government. However, a company may issue equity shares with differential rights upon expiry of five years from the end of the financial year in which such default was made good.
- (h) the company has not been penalized by Court or Tribunal during the last three years of any offence under the Reserve Bank of India Act, 1934, Securities and Exchange Board of India Act, 1992, Securities Contracts (Regulation) Act, 1956, the Foreign Exchange Management Act, 1999 or any other special Act under which such companies being regulated by sectoral regulators.
- (i) The explanatory statement to be annexed to the notice of the general meeting should contain the disclosures as mentioned in the rules
- (j) The Board of Directors shall disclose in the Board's Report for the financial year in which the issue of equity shares with differential rights was completed, the details as mentioned in the rules

The holders of the equity shares with differential rights shall enjoy all other rights such as bonus shares, rights shares etc., which the holders of equity shares are entitled to, subject to the differential rights with which such shares have been issued.
- (k) The company shall not convert its existing share capital with voting rights into equity share capital carrying differential voting rights and *vice-versa*.
- (l) The register of members maintained under section 88 of the Companies Act, 2013, shall contain all the relevant particulars of the shares so issued along with details of the shareholders.

PREFERENCE SHARES

According to explanation (ii) to Section 43 of Companies Act, 2013 "preference share capital", with reference to any company limited by shares, means that part of the issued share capital of the company which carries or would carry a preferential right with respect to –

- (a) payment of dividend, either as a fixed amount or an amount calculated at a fixed rate, which may either be free of or subject to income-tax; and
 - (b) repayment, in the case of a winding up or repayment of capital, of the amount of the share capital paid-up or deemed to have been paid-up, whether or not, there is a preferential right to the payment of any fixed premium or premium on any fixed scale, specified in the memorandum or articles of the company;
- (iii) capital shall be deemed to be preference capital, notwithstanding that it is entitled to either or both of the following rights, namely:–
- (a) that in respect of dividends, in addition to the preferential rights to the amounts specified in sub-clause (a) of clause (ii), it has a right to participate, whether fully or to a limited extent, with capital not entitled to the preferential right aforesaid;
 - (b) that in respect of capital, in addition to the preferential right to the repayment, on a winding up, of the amounts specified in sub-clause (b) of clause (ii), it has a right to participate, whether fully or to a limited extent, with capital not entitled to that preferential right in any surplus which may remain after the entire capital has been repaid.

In simple terms, the preference shares are those shares which have rights of preference over equity shares in

the case of distribution of dividend and distribution of surplus in the case of winding up. They generally carry a fixed rate of dividend and redeemable after specific period of time. According to Section 55 of the Companies Act, 2013, a Company cannot issue preference shares which are irredeemable.

The following kinds of preference shares are issued by the companies:

- Cumulative preference shares
- Non-cumulative preference shares
- Convertible preference shares
- Redeemable preference shares
- Participating preference share
- Non participating preference shares

CUMULATIVE PREFERENCE SHARES

Cumulative preference shares where the preference dividend gets accumulated for being paid subsequently if the company does not have adequate profits. Such arrears of dividend need to be paid in subsequent years before payment of equity dividends.

NON-CUMULATIVE PREFERENCE SHARES

In the case of these preference shares, dividend does not accumulate. If there are no profits or the profits are inadequate in any year, the shares are not entitled to any dividend for that year. Unless there is a specific provision in the Articles of Association of the company, the preference shareholders have no right to participate in the surplus profits or in the surplus assets in a winding up. RBI also allowed Indian banks to issue these types of preference shares as capital under Basel III capital regulations.

CONVERTIBLE PREFERENCE SHARES

If the terms of issue of preference shares includes a right for converting them into equity shares at the end of a specified period they are called convertible preference shares. In the absence of such condition or right, the preference shares are not converted into equity shares to become eligible for various rights such as voting, higher dividend, bonus issue etc. as in the case of equity shares. These shares are some times referred to as quasi equity shares in common parlance.

REDEEMABLE PREFERENCE SHARES

These are such preference shares in which are redeemed after specific period and money is returned to shareholders. According to Section 55 of the Companies Act, 2013, a Company cannot issue preference shares which are irredeemable. If Article of association permits, the Company can issue preference shares which are redeemable not later than 20 years. Companies engaged in infrastructure projects can issue shares redeemable exceeding 20 years subject to condition mentioned in rule 9 and 10 of the Companies (Share Capital and Debenture) Rules, 2014.

PARTICIPATING PREFERENCE SHARES

Preference shareholders are not entitled to dividend more than what has been indicated as part of the terms of issue, even in a year in which the company has made huge profits. Subject to provision in the terms of issue these shares can be entitled to participate in the surplus profits left, after payment of dividend to the preference and the equity shareholders to the extent provided therein. Subject to provisions in the terms of issue such preference shares can be entitled even to bonus shares.

NON PARTICIPATING PREFERENCE SHARES

Unless the terms of issue indicate specifically otherwise, all preference shares are to be regarded as non-participating preference shares.

FULLY CONVERTIBLE CUMULATIVE PREFERENCE SHARE (EQUIPREF)

This instrument is in two parts A & B. Part A is convertible into equity shares automatically and compulsorily on the date of allotment without any application by the allottee, and Part B is redeemed at par/ converted into equity after a lock in period at the option of the investor, at a price 30% lower than the average market price. The dividend is given only for part B shares.

DEBENTURES

Section 2(30) of the Companies Act, 2013 defines debentures. “Debenture” includes debenture stock, bonds or any other instrument of a company evidencing a debt, whether constituting a charge on the assets of the company or not;

Debenture is a document evidencing a debt or acknowledging it and any document which fulfills either of these conditions is a debenture.

The important features of a debenture are:

1. It is issued by a company as a certificate of indebtedness.
2. It usually indicates the date of redemption and also provides for the repayment of principal and payment of interest at specified date or dates.
3. It usually creates a charge on the undertaking or the assets of the company. In such a case the lenders of money to the company enjoy better protection as secured creditors, i.e. if the company does not pay interest or repay principal amount, the lenders may either directly or through the debenture trustees bring action against the company to realise their dues by sale of the assets/undertaking earmarked as security for the debt.
4. Debentures holders does not have any voting rights.
5. Compulsory payment of interest. The interest on debenture is payable irrespective of whether there are profits made or not.

TYPES OF DEBENTURES

Naked or unsecured debentures	Debentures of this kind do not carry any charge on the assets of the company.
Secured debentures	Debentures that are secured by a mortgage of the whole or part of the assets of the company are called mortgage debentures or secured debentures.
Redeemable debentures	Debentures that are redeemable on expiry of certain period are called redeemable debentures.
Perpetual debentures	If the debentures are issued subject to redemption on the happening of specified events which may not happen for an indefinite period, e.g. winding up, they are called perpetual debentures.
Bearer debentures	Such debentures are payable to bearer and are transferable by mere delivery.

Registered debentures	Such debentures are payable to the registered holders whose name appears on the debenture certificate/ letter of allotment and is registered on the companies register of debenture holders maintained as per Section 88(1)(b) of the Companies Act, 2013.
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CATEGORIES OF DEBENTURES

Based on convertibility, debentures can be classified under three categories:

1. Fully Convertible Debentures (FCDs)
2. Non Convertible Debentures (NCDs)
3. Partly Convertible Debentures (PCDs)

FULLY CONVERTIBLE DEBENTURES

These are converted into equity shares of the company with or without premium as per the terms of the issue, on the expiry of specified period or periods. If the conversion is to take place at or after eighteen months from the date of allotment but before 36 months, the conversion is optional on the part of the debenture holders in terms of SEBI (ICDR) Regulations. Interest will be payable on these debentures upto the date of conversion as per transfer issue.

NON CONVERTIBLE DEBENTURES (NCDs)

These debentures do not carry the option of conversion into equity shares and are therefore redeemed on the expiry of the specified period or periods.

PARTLY CONVERTIBLE DEBENTURES (PCDs)

These may consist of two kinds namely -convertible and non-convertible. The convertible portion is to be converted into equity shares at the expiry of specified period. However, the non convertible portion is redeemed at the expiry of the stipulated period. If the conversion takes place at or after 18 months, the conversion is optional at the discretion of the debenture holder.

BASIC FEATURES OF CONVERTIBLE DEBENTURES

- Debentures are issued for cash at par.
- They are converted into specified or unspecified number of equity shares at the end of the specified period. The ratio at which the convertible debentures are exchanged for equity shares is known as conversion price or conversion ratio which is worked out by dividing the face value of a convertible debenture by its conversion price. For instance if the face value of a convertible debenture is ₹ 100 and it is convertible into two equity shares, the conversion price is ₹ 50 and the conversion ratio is 2. The difference between the conversion price and the face value of the equity share is called conversion premium.
- Convertible debentures may be fully or partly convertible. In case it is fully convertible the entire face value is converted into equity shares on expiry of the stipulated period. If partly convertible, the convertible portion is converted into equity shares on expiry of the specified period and the non convertible portion is redeemed at the expiry of certain period.
- Conversion into equity shares may take place in one or more stages at the end of specified period or periods in the case of fully or partly convertible debentures.
- If one or more parts of the debentures are convertible after 18 months, a company should get a credit

rating done by a credit rating agency approved by SEBI. Fresh rating is required if debentures are rolled over.

- Convertible debentures of public companies are listed on the stock exchanges to assure liquidity to the holders. However, even today debt instruments are not actively traded in Indian stock exchanges.

ADVANTAGES OF CONVERTIBLE DEBENTURES

The advantages of convertible debentures to the company are –

1. Capitalisation of interest cost till the date of commissioning of the project is allowed in accordance with accounting principle. If the conversion of the debentures is duly linked with the commissioning of the project the entire interest cost can be capitalised, without charging the interest to profit & loss account and pulling down the profits of the company.
2. Convertible debentures carry lower interest as compared to the rate charged by the Banks and Financial Institutions.
3. From the point of view of the debt equity ratio the convertible part of the debentures is treated as equity by financial institutions. The company is thus enabled to have a high degree of flexibility in financing its future projects.
4. Equity capital gets increased after each conversion, facilitating easier servicing of equity by payment of dividend.
5. Tax benefits are higher as interest on debentures is allowed as a deduction in computation of taxable income of the company. Additionally a company having a proven track record and future earning potential will be able to charge reasonable premium at the time of conversion.
6. In the case of term loans from FIs and Banks they usually impose many conditions on management including placing their representative on the board. In the case of convertible debentures there is thus a greater degree of autonomy for the companies.

The advantages of the convertible debentures to the investors are –

1. The investor is assured of a fixed return by way of interest on the debentures till conversion. On conversion into equity the investor becomes entitled to receive dividend declared on equity shares. The advantage to the investor is that he receives a fixed return on his investment by way of interest even during the gestation period and project implementation period.
2. As price of equity shares tends to rise on completion of the project of the company, the investor gets value appreciation on his investment, if converted into equity.
3. In most cases, debentures carry security with a charge on all or a part of movable/immovable properties of the company. This assures prompt payment of principal and interest by invoking the assistance of a debenture trustee. However in terms of SEBI Regulations where the debentures have a maturity period of 18 months or less it is mandatory for the company to create security on the debentures.
4. A fair amount of liquidity is enjoyed by convertible debentures listed on the stock exchanges depending on the track record of the companies. Even if debentures are not traded as actively as equity shares, convertible debentures of good companies command reasonable liquidity. Where a debenture has several parts, each part of the convertible debentures can be traded separately or in full on the stock exchanges.
5. The following options are available to the investor who has bought convertible debentures issued in several parts:

- (a) To sell all the parts immediately on allotment;
- (b) To sell one or more parts and retain other or others till conversion and to obtain equity shares for retention or sale.

DISTINCTION BETWEEN FULLY CONVERTIBLE AND PARTLY CONVERTIBLE DEBENTURES

<i>Characteristics</i>	<i>Partly convertible debentures</i>	<i>Fully convertible debentures</i>
Suitability	Better suited for companies with established track record	Better suited for companies without established track record
Capital base	Relatively lower equity capital on conversion of debentures	Higher equity capital on conversion of debentures
Flexibility in financing	Favourable debt equity ratio	Highly favourable debt equity ratio
Classification for debt-equity ratio computation	Convertible portion classified as 'equity' and non-convertible portion as 'debt'	Classified as equity for debt-equity computation
Popularity	Not so popular with investors	Highly popular with investors
Servicing of equity	Relatively lesser burden of equity servicing	Higher burden of servicing of equity

In the case of partly convertible debentures, debenture redemption reserve has to be created for 50% of the face value of the non-convertible portion. The facility of buy-back is also permissible in respect of non-convertible portion of debentures.

In contrast no reserve for debenture redemption is required for fully convertible debentures nor are buy-back arrangements permissible.

Sometimes companies issue zero interest fully convertible debentures. In this case, investors are not paid any interest till the date of conversion or upto the notified date, after which they are converted into shares. For the investor the investment amount is lower and cost of conversion also is less. Further this helps them as a means of tax planning since interest which is otherwise taxable is not paid. The capital appreciation at the time of conversion is treated as capital gains where tax rate is less. Companies also prefer this instrument because they are able to avoid payment of interest.

FULLY CONVERTIBLE DEBENTURES WITH INTEREST (OPTIONAL)

In this case there is no interest payment involved say for the first 6 months. Then the holder can exercise option and apply for securities at a premium without paying additional amount. However interest will be payable at a determined rate from the date of first conversion to second/final conversion and in lieu thereof equity shares are issued.

Upon conversion of each part, the face value stands reduced proportionately on the date of conversion.

SWEAT EQUITY SHARES

Section 2 (88) of the Companies Act, 2013 defines "sweat equity shares" means such equity shares as are issued by a company to its directors or employees at a discount or for consideration, other than cash, for providing their know-how or making available rights in the nature of intellectual property rights or value additions, by whatever name called.

Company issue shares at a discount or for consideration other than cash to selected employees and directors as per norms approved by the Board of Directors or any committee, like compensation committee, formed for this purpose. This is based on the know how provided or intellectual property rights created and given for value additions made by such directors and employees to the company.

It may be noted that the intellectual property right, know how or value additions arise as of now mainly in the case of Information Technology related companies and Pharmaceutical companies. Categories of industries which are eligible to issue sweat equity shares have not been indicated by the Government either in the Act or otherwise.

According to Section 54 of the Companies Act, 2013 a company may issue sweat equity shares of a class of shares already issued, if the following conditions are fulfilled:

- (a) The issue is authorized by a special resolution passed by the company in the general meeting.
- (b) The resolution specifies the number of shares, current market price, consideration if any and the class or classes of directors or employees to whom such equity shares are to be issued.
- (c) Not less than one year has elapsed at the date of the issue, since the date on which the company was entitled to commence business.
- (d) The sweat equity shares of a company whose equity shares are listed on a recognised stock exchange are issued in accordance with the regulations made by SEBI in this regard and if they are not listed the sweat equity shares are to be issued in accordance with the rule 8 of Companies (Share Capital and Debenture) Rules, 2014.

SECURED PREMIUM NOTES

These instruments are issued with detachable warrants and are redeemable after a notified period say 4 to 7 years. The warrants enable the holder to get equity shares allotted provided the secured premium notes are fully paid. It combines the feature of both debt and equity. During the lock in period no interest is paid. The holder has an option to sell back the SPN to the company at par value after the lock in period. If the holder exercises this option, no interest/premium is paid on redemption. In case the holder keeps it further, he is repaid the principal amount along with the additional interest/premium on redemption in installments as per the terms of issue. The conversion of detachable warrants into equity has to be done within the specified time. TISCO took the lead in July, 1992 by making a mega rights issue of equity shares and secured premium notes aggregating to ₹ 1,212 crores.

The terms of the SPN were so formulated that the return on investment was treated as capital gain and not regular income. Consequently, the rate of tax applicable was lower.

EQUITY SHARES WITH DETACHABLE WARRANTS

The holder of the warrant is eligible to apply for the specified number of shares on the appointed date at the pre-determined price. These warrants are separately registered with the stock exchanges and traded separately. The practice of issuing non convertible debentures with detachable warrants also exists in the Indian market.

DUAL OPTION WARRANTS

Dual option warrants are designed to provide the buyer with good potential of capital appreciation and limited downside risk. Dual option warrants may be used to sell equity shares in different markets. For example, equity shares or debentures may be issued with two warrants - one warrant giving right to the purchaser to be allotted one equity share at the end of a certain period and another warrant with a debt or preference share option.

DEBT INSTRUMENTS WITH DEBT WARRANTS

Debt instruments may be issued with debt warrants which give the holder the option to invest in additional debt on the same terms within the period specified in the warrant. This instrument is beneficial to the investors in periods of falling interest rates when the holder can exercise the debt warrant option and hold additional debt at interest rates above market rates.

DEBT FOR EQUITY SWAP

These instruments give an offer to the debt holders to exchange the debt for equity shares of the company.

The issuers offering debt for equity swaps are interested in increasing equity capital by improving their debt-equity ratios and enhancing their debt issuing capacity. They reduce their interest burden and replace it with dividend burden which is payable at the discretion of the issuer. However, the issuer faces the risk of dilution of earnings per share by a sharp rise in the equity. In addition, dividends are not tax deductible.

From the investors' point of view, there is potential gain from rise in the value of the equity shares. The potential rise in price of equity shares may or may not materialize.

Variations of this instrument are mortgage backed securities that split the monthly payment from underlying mortgages into two parts -each receiving a specified portion of the principal payments and a different specified portion of the interest payments.

INDEXED RATE NOTES

In indexed rate notes, the interest rate fixation is postponed till the actual date of placement, rather than fixing it on the date of the commitment. The interest rate is computed on the date of take down at the prevailing private placement rates, using a formula based on the index such as the 182 days treasury bill yield rates. These instruments are beneficial to a company in a high interest rate environment, if the interest rates are expected to decline between the date of commitment and the date of take down.

EXTENDABLE NOTES

Extendable notes are issued for 10 years with flexibility to the issuer to review the interest rate every two years. The interest rate is adjusted every two years to reflect the prevailing market conditions by trying the interest rate to a spread over a bond index such as two years treasury notes. Depending on the specific terms of the extendable bond, the bond holder and/or bond issuer may have one or more opportunities to defer the repayment of the bond's principal, during which time interest payments continue to be paid. Additionally, the bond holder or issuer may have the option to exchange the bond for one with a longer maturity, at an equal or higher rate of interest. Because these bonds contain an option to extend the maturity period, a feature that adds value to the bond, extendable bonds sell at a higher price than non-extendable bonds.

LEVEL PAY FLOATING RATE

Level pay floating rate notes are issued for a long period of time say 20 years, with adjustment in interest rate every five years. These notes provide for level payments for time intervals during the term of the note, with periodic interest adjustments tied to an index, and adjustments to the principal balance to reflect the difference between the portion of the payment allocable to interest and the amount of floating rate interest actually incurred. Maximum limits on upward adjustments to principal are specified at the outset to protect the lender from runaway floating exposure. The level pay note has the advantage to the issuer of having a predictable level of debt service for a period of years, thereby avoiding the uncertainties of floating debt on cash flows during that time.

ZERO COUPON CONVERTIBLE NOTES

These are debt convertible into equity shares of the issuer. If investors choose to convert, they forgo all the accrued and unpaid interest. These convertibles are generally issued with put option to the investors. The advantage to the issuer is the raising of convertible debt without heavy dilution of equity. Since the investors give up acquired interest by exercise of conversion option, the conversion option may not be exercised by many investors.

The investor gains in the event of appreciation in the value of the equity shares. Even if the appreciation does not materialize, the investor has the benefit of a steady stream of implied income. If the instrument is issued with put option, the investor can resell the securities to the investor.

DEEP DISCOUNT BOND

IDBI and SIDBI had issued this instrument. For a deep discount price of ₹ 2,700/- in IDBI the investor got a bond with the face value of ₹ 1,00,000. The bond appreciates to its face value over the maturity period of 25 years. Alternatively, the investor can withdraw from the investment periodically after 5 years. The capital appreciation is charged to tax at capital gains rate which is lower than normal income tax rate. The deep discount bond is considered a safe, solid and liquid instrument and assigned the best rating by CRISIL.

DISASTER BONDS

These are issued by companies and institutions to share the risk and expand the capital to link investors return with the size of insurer losses. The bigger the losses, the smaller the return and vice-versa. The coupon rate and the principal of the bonds are decided by the occurrence of the casualty of disaster and by the possibility of borrower defaults.

OPTION BONDS

This instrument covers those cumulative and non-cumulative bonds where interest is payable on maturity or periodically and redemption premium is offered to attract investors.

EASY EXIT BONDS

This instrument covers both bonds which provide liquidity and an easy exit route to the investor by way of redemption or buy back where investors can get ready encashment in case of need to withdraw before maturity.

PAY IN KIND BONDS

This refers to bonds wherein interest for the first three to five years is paid through issue of additional bonds, which are called baby bonds as they are derived from parent bond.

SPLIT COUPON DEBENTURES

This instrument is issued at a discounted price and interest accrues in the first two years for subsequent payment in cash. This instrument helps better management of cash outflows in a new project depending upon cash generating capacity.

FLOATING RATE BONDS AND NOTES

In this case interest is not fixed and is allowed to float depending upon market conditions. This instrument is used by the issuers to hedge themselves against the volatility in interest rates.

Some of the above instruments have been used selectively by companies and institutions recently to raise funds.

CLIP AND STRIP BONDS

Clip and strip bonds also referred to as coupon notes, split the principal and coupon portions of a bond issue and two separate coupon instruments are sold to the investors.

In structuring a coupon note issue, a conventional current coupon bond is sold to the investor. The streams of coupon payments are stripped away and the principal amount of bond is sold as a deep discount bond. The gain to the investor is difference between the purchase price and the par value. The coupon streams are sold like zero coupon bonds where the investor pays discount for it and receives the payment at a lower rate.

DUAL CONVERTIBLE BONDS

A dual convertible bond is convertible into either equity shares or fixed interest rate debentures/preference shares at the option of the lender. Depending on the prospects of the project during the conversion period, the lender may exercise either of the options. The fixed interest rate debenture may have certain additional features including higher rate of interest distinct from the original debt instrument.

STEPPED COUPON BONDS

Under stepped coupon bonds, the interest rate is stepped up or down during the tenure of the bond. The main advantage to the investor is the attraction of higher rate of interest in case of general rise in interest rates.

INDUSTRIAL REVENUE BONDS

Industrial revenue bonds are issued by financial institutions in connection with the development or purchase of industrial facilities. These may become attractive if certain income-tax and wealth-tax concessions are offered.

The bond proceeds could be used to purchase or a construct facilities which are subsequently leased or sold to the company. The institution acts as a conduit of funds between the lenders and the company in order to take advantage of tax benefits enjoyed by the institutions.

COMMODITY BONDS

Commodity bonds are bonds issued to share the risk and profitability of future commodity prices with the investor. For example, petro bonds, silver bonds, gold bonds and coal bonds.

A petro bond may carry a fixed rate of interest with part of the face value of the bonds denominated in barrels of oil. There would be a floor in the face value of the bond. In view of the upside profit potential in oil prices, the interest rate could be lower than the market rate of interest. These bonds may be issued for decontrolled items.

CARROT AND STICK BOND

Another variation of the above instrument is the carrot and stick bond. The carrot is the lower than normal conversion premium i.e. the premium over the present market price of the equity shares is fixed at a reasonable level so that the price of the equity shares need not increase significantly to make conversion practical. The stick is the issuer's right to call the issue at a specified premium if the price of the equity shares is traded above a specified percentage of the conversion price.

CAPITAL INDEXED BONDS

Capital indexed bonds are inflation-protection securities. Such bonds, therefore, provide good hedge against inflation risk. The benefits do extend beyond hedging. Capital index bonds can be used as a market indicator for inflation expectation. This will help investors take a more intelligent decision on their current consumption. Finally, the spot yield curve can be better constructed based on the real yields.

Inflation risk: A nominal bond is exposed to high inflation risk. This is the risk that inflation will increase, leading to increase in interest rate. Essentially then, inflation risk is a sub-component of interest rate risk. A capital

indexed bonds lowers the interest rate risk by neutralizing the inflation risk.

The effectiveness of the hedge will, however, depend on the appropriateness of the inflation index. The purpose of issuing capital indexed bonds will not be fully served if the RBI were to use the Wholesale Price Index (WPI) or the Retail Price Index (RPI) as the index for inflation. The reason is that these indices do not adequately capture inflation as it affects the investors, especially the retail class.

If banks are protected against inflation risk, they may, perhaps, pass on the benefits in the form of higher interest rate to the retail investors. That, in turn, provides retail investors a higher cushion against inflation risk. In such cases, more the inflation index is aligned to price levels affecting retail consumption, better the hedge.

Inflation expectation: Investors buy bonds by postponing their current consumption. There is, therefore, a trade-off between investment and consumption. To make an intelligent decision between these two states of nature, investors need an indicator to measure inflation expectations. At present, due to lack of adequate measures, we assume that inflation expectation is the same as current inflation. If actual inflation were higher in the future, the investment decision may be unattractive. It is, therefore, important to proxy inflation expectation. A capital indexed bond helps in this regard.

If the RBI were to issue capital indexed bonds across the yield curve, we will have real yields for each maturity sector. We already have nominal yields as well for these sectors. The difference between the nominal and the real yields is a proxy for inflation expectation.

INFLATION INDEXED BONDS OR INFLATION INDEXED NATIONAL SAVINGS SECURITIES

India recently launched a new kind of bond to give individual investors some protection against inflation. The new bonds, officially called the Inflation Indexed National Savings Securities.

Unlike a traditional bond where the interest rate is fixed, in the inflation-linked bonds, the government will pay an interest of 1.5% per year above the rate of inflation as measured by the Consumer Price Index.

The interest rate will be reset every six months, to reflect any changes in inflation.

These bonds aren't a great deal for investors who are in higher income-tax brackets, because the interest on the bonds is taxable as income. After taxes, the returns on these bonds will be lower than inflation.

TAX FREE BONDS

Specified Companies issue Tax free bonds. The interest paid on this bonds are tax free in the hand of investor.

GLOBAL DEPOSITORY RECEIPTS

According to Section 2 (44) of the Companies Act, 2013 "Global Depository Receipt" means any instrument in the form of a depository receipt, by whatever name called, created by a foreign depository outside India and authorised by a company making an issue of such depository receipts;

Section 41 of the Companies Act, 2013 authorizes a company to issue Global Depository Receipts after following the conditions as prescribed in Companies (Issue of Global Depository Receipts) Rules, 2014.

It is a form of depository receipt or certificate created by the Overseas Depository Bank outside India denominated in dollar and issued to non-resident investors against the issue of ordinary shares or foreign currency convertible bonds of issuing company. In simple words, it is basically a negotiable instrument denominated in US dollars. It is traded in Europe or the US or both. After getting approval from the Ministry of Finance and completing other formalities, a company issues rupee denominated shares in the name of depository which delivers these shares to its local custodian bank, the holder on records, thus depository. The depository then issues dollar denominated depository receipts (or GDR) against the shares registered with it. Generally one GDR is equivalent to one or more (rupee denominated) shares. It is traded like any other dollar denominated security in the foreign markets,

in addition to equity financing (as GDR represents equity) over debt financing. GDR issue also possesses merits like less issue formalities, less administrative works as regards dividend payment, information dissemination, annual general meeting etc. as the issuer deal only with a single shareholder, the depository; easy availability of foreign exchange and no foreign exchange risk. Besides issuing companies, foreign investors especially FIIs also get advantage of investing in the Indian companies without getting registration with SEBI, relief from cumbersome settlement and delivery procedures, adequate liquidity (as GDR is as liquid as the shares of the company in its home market) and generally higher returns. In fact, GDR holders enjoy all economic benefits of the underlying shares but have none of the corporate rights like right to vote.

FOREIGN CURRENCY CONVERTIBLE BOND (FCCB)

A Foreign Currency Convertible Bond (FCCB) is a quasi debt instrument which is issued by any corporate entity, international agency or sovereign state to the investors all over the world. They are denominated in any freely convertible foreign currency. Euro Convertible Bonds are usually issued as unsecured obligation of the borrowers. FCCBs represent equity linked debt security which can be converted into shares or into depository receipts. The investors of FCCBs has the option to convert it into equity normally in accordance with pre-determined formula and sometimes also at a pre-determined exchange rate. The investor also has the option to retain the bond. The FCCBs by virtue of convertibility offers to issuer a privilege of lower interest cost than that of similar non convertible debt instrument. By issuing these bonds, a company can also avoid any dilution in earnings per share that a further issue of equity might cause whereas such a security still can be traded on the basis of underlying equity value. The agreement providing for the issuance of FCCBs normally carry less restrictive covenants as they relate to the issuer. Further, FCCBs can be marketed conveniently and the issuer company can expect that the number of its shares will not increase until investors see improved earnings and prices for its common stock. Like GDRs, FCCBs are also freely tradeable and the issuer has no control over the transfer mechanism and cannot be even aware of ultimate beneficiary. The Finance Ministry vide Notification dated 20.6.1994 stated that w.e.f. this date FCCBs will be considered an approved instrument of accessing external commercial borrowings. The terms and conditions normally applicable to commercial borrowing would be binding on convertible bonds. This would include restrictions on end-use, import of capital goods and minimum maturity for bonds. Priority for accessibility to this facility would be given to firms with good forex earnings record or potential.

INDIAN DEPOSITORY RECEIPTS

According to Section 2(48) of the Companies Act, 2013 “Indian Depository Receipt” means any instrument in the form of a depository receipt created by a domestic depository in India and authorised by a company incorporated outside India making an issue of such depository receipts;

Section 390 of the Companies Act, 2013 and rule 13 of Companies (Registration of Foreign Companies) Rules, 2014 lays down the procedure for issue of Indian Depository Receipts.

Apart from this a company has to comply with Chapter X and XA of SEBI (ICDR) Regulations, 2009 to issue IDRs or a rights issue of IDRs.

An IDR is an instrument denominated in Indian Rupee in the form of a depository receipt created by a domestic depository (Custodian of securities registered with SEBI) against the underlying equity of issuing company to enable foreign companies to raise funds from Indian Securities Markets.

In an IDR, foreign companies would issue shares, to a domestic (Indian) depository, which would in turn issue depository receipts to investors in India. The actual shares underlying the IDRs would be held by an Overseas Custodian, which shall authorize the Indian depository to issue the IDRs. To that extent, IDRs are derivative instruments because they derive their value from the underlying shares. Standard Chartered PLC is only company to offer IDR in the Indian market.

Benefits to the stakeholders

Issuing Companies: Any foreign company listed in its home country and satisfying the eligibility criteria can issue IDRs. A company which has significant businesses in India can increase its value through IDRs by breaking down market segmentations, reaching trapped pools of liquidity, achieving international shareholder base and improving its brand's presence through global visibility.

Investors: IDRs can lead to better portfolio management and diversification for investor by giving them a chance to buy into the stocks of reputed companies abroad.

TRACKING STOCKS

A Tracking stock is a type of common stock that “tracks” or depends on the financial performance of a specific business unit or operating division of a company, rather than the operations of the company as a whole. As a result, if the unit or division performs well, the value of the tracking stocks may increase, even if the company's performance as a whole is not up to mark or satisfactory. The opposite may also be true.

A tracking stock is a special type of stock issued by a publicly held company to track the value of one segment of that company. By issuing a tracking stock, the different segments of the company can be valued differently by investors. Tracking stocks are generally issued by a parent company in order to create a financial vehicle that tracks the performance of a particular division or subsidiary. When a parent company issues a tracking stock, all revenues and expenses of the applicable division are separated from the parent company's financial statements and bound to the tracking stock. Often this is done to separate a high-growth division from large losses shown by the financial statements of the parent company. The parent company and its shareholders, however, still control operations of the subsidiary.

Tracking stock carries dividend rights tied to the performance of a targeted division without transferring ownership or control over divisional assets. In contrast to a spin-off or an equity carve-out, the parent retains full control, allowing it to enjoy any operating synergies, or economies of scale in administration or finance.

Shareholders of tracking stocks have a financial interest only in that unit or division of the company. Unlike the common stock of the company itself, a tracking stock usually has limited or no voting rights. In the event of a company's liquidation, tracking stock shareholders typically do not have a legal claim on the company's assets. If a tracking stock pays dividends, the amounts paid depends on the performance of the business unit or division. But not all tracking stocks pay dividends.

A company has many good reasons to issue a tracking stock for one of its subsidiaries (as opposed to spinning it off to shareholders).

- (i) First, the company keeps control over the subsidiary (although they don't get all the profit), but all revenues and expenses of the division are separated from the parent company's financial statements and attributed to tracking stock. This is often done to separate a high growth division with large losses from the financial statements of the parent company.
- (ii) Second, they might be able to lower their costs of obtaining capital by getting a better credit rating.
- (iii) Third, the businesses can share marketing, administrative support functions, etc.
- (iv) Finally, if the tracking stock shoots up, the parent company can make acquisitions and pay in stock of subsidiary instead of cash.

When a tracking stock is issued, the company can choose to sell it to the markets (i.e., via an initial public offering) or to distribute new shares to existing shareholders. Either way, the newly tracked business segment gets a longer lease, but can still run back to the parent company in tough times.

ADVANTAGES OF TRACKING STOCK

A key advantage of tracking stock is that it offers divisional managers a degree of decision-making authority that might otherwise be unattainable, given top management's reluctance to dilute its control over the division's assets. The practical effect should be to enhance job satisfaction for divisional managers, thus reducing retention risk and also increasing the company's responsiveness to changing market conditions. Also, investors have more direct access to the specific businesses of the parent, which can be highly useful in the case of a diversified company. Another possible reason for the growing popularity of trackers is that trackers allow mainstream companies to exploit the dual stock market pricing between conventional and high-tech or Internet businesses. By creating tracked business units, conventional businesses too can benefit from the pricing frenzy.

DISADVANTAGES OF TRACKING STOCK

For investors, tracking stocks can be of a mixed bag. Like regular stocks, tracking stockholders are entitled to dividends paid out by the subsidiaries issuing the tracking stock. Yet the holders of tracking stocks do not have ownership in the company, instead, at-times tracking stock shareholders vote on issues affecting the corporate parent, not the subsidiary whose stocks they own. Another downside is the fact that the board of directors of the tracking-stock subsidiary is often put in place by the parent company and is not elected by tracking stock shareholders, which would cause conflicts of interests.

The tracking stocks are highly skeptical also. Shareholders have limited voting rights, if any, and they cannot elect their own boards. Moreover, if the parent company falls on hard times, conflict could develop between the shareholders of a tracked division, especially if it continues to do well, and the shareholders of the parent company. The potential for such conflict could affect the performance of the tracking stock.

Another important drawback with tracking stock is that it can dramatically increase the potential for conflict and litigation over accounting policy. It is because the owners of the tracking stock have rights only over dividends, and dividend payouts are driven by the recognition of divisional profits, the arguments over profit recognition are almost sure to arise whenever tracking stock investors are disappointed in their returns. They will surely be tempted to accuse corporate management of adopting policies that deliberately understate their profits.

MORTGAGE BACKED SECURITIES

These securities assure a fixed return which is derived from the performance of the specific assets. They are issued with a maturity period of 3 to 10 years and backed by pooled assets like mortgages, credit card receivables, etc. There is a commitment from the loan originator and/or intermediary institution to ensure a minimum yield on maturity.

FEATURES OF ASSETS TO BE SECURITISED

The assets to be securitized shall have the following features:

- (a) The cash flows generated from the assets should be received periodically in accordance with a pre-determined schedule.
- (b) The actual cash flows generated from the assets should be predictable.
- (c) The assets should be large in number and total value to be issued in securitized form.
- (d) The assets should be sufficiently similar in nature to enable pooling of their cash flows.
- (e) The assets should be marketable.

Advantages of Asset backed Securities to Issuer

- (a) The issuer can generate cash from the assets immediately enabling funds to be redeployed in other projects.

- (b) The issuer may be able to improve balance sheet ratios by excluding the original assets and the securities created by the assets from the balance sheet by suitable structuring of the transaction.

Advantages of Asset backed Securities to Investor

These instruments have a relatively low credit risk since the securities are backed by good quality collateral and offer a higher yield than Government securities.

FUTURES

Futures is a contract between two parties to buy or sell a underlying asset of standardized quantity and quality for a price agreed upon today with delivery and payment occurring at a specified future date. Underlying assets for the purpose include equities, foreign exchange, interest bearing securities and commodities. The idea behind financial futures contract is to transfer future changes in security prices from one party in the contract to the other. It offers a means to manage risk in participating financial market. Futures basically transfer value rather than create it. It is a means for reducing risk or assuming risk in the hope of profit. Every futures contract entered into has two side willing buyer and a willing seller. If one side of contract makes a profit, the other side must make a loss. All futures market participants taken together can neither lose nor gain the futures market is a zero sum game.

OPTIONS

An option contract conveys the right, but not the obligation, to buy or sell a specific security or commodity at specified price within a specified period of time. The right to buy is referred to as a call option whereas the right to sell is known as a put option. An option contract comprises of its type a put or call, underlying security or commodity expiry date, strike price at which it may be exercised.

Option provides the investor with the opportunity to hedge investments in the underlying shares and share portfolios and can thus reduce the overall risk related to the investments significantly. Generally two type of options namely :

- European option – an option that may only be exercised on expiration.
- American option – an option that may be exercised on any trading day on or before expiry.

Term one should know

- **Long Position** – A position showing a purchase or a greater number of purchase than sales in anticipation of a rise in prices. A long position can be closed out through the sale of an equivalent amount.
- **Short Position** – In futures, the short has sold the commodity or security for future delivery; in options, the short has sold the call or put and is obligated to take a futures position if he or she is assigned for exercise.

HEDGE FUNDS

Hedge funds, including fund of funds are unregistered private investment partnerships, funds or pools that may invest and trade in many different markets, strategies and instruments (including securities, non-securities and derivatives) and are not subject to the same regulatory requirements as mutual funds, including mutual fund requirements to provide certain periodic and standardized pricing and valuation information to investors.

The term can also be defined by considering the characteristics most commonly associated with hedge funds. Usually, hedge funds:

- are organized as private investment partnerships or offshore investment corporations;
- use a wide variety of trading strategies involving position-taking in a range of markets;

- employ as assortment of trading techniques and instruments, often including short-selling, derivatives and leverage;
- pay performance fees to their managers; and
- have an investor base comprising wealthy individuals and institutions and relatively high minimum investment limit

Hedge Fund and Other Pooled Investment Vehicles

Hedge funds are sometimes called as ‘rich man’s mutual fund’. In addition, other unregistered investment pools, such as venture capital funds, private equity funds and commodity pools, are sometimes referred to as hedge funds. Although all of these investment vehicles are similar in that they accept investors’ money and generally invest it on a collective basis, they also have characteristics that distinguish them from hedge funds.

Mutual Fund or Registered Investment Companies

In many ways, hedge funds are similar to mutual funds. Both entities issue units or securities to investors, hold pools of securities to diversify investment, have professional asset manager and may, at times, have similar investment strategies. At the same time, they also differ in a number of ways. Mutual funds are registered with securities markets regulator and are subject to the provisions of the relevant regulations such as, offer/issue of units/securities, disclosure and reporting requirement, valuation for the purpose of computation of NAV, conflict of interest issue and limit leverage. Hedge funds are not required to be registered and therefore, are not subject to similar regulatory provisions.

Private Equity Fund

A private equity fund, like a hedge fund, is an unregistered investment vehicle in which investors pool money to invest. Private equity funds concentrate their investments in unregistered (and typically illiquid) securities. Like hedge funds, private equity funds also rely on the exemption from registration of the offer and sale of their securities. The investors in private equity funds and hedge funds typically include high net worth individuals and families, pension funds, endowments, banks and insurance companies. Private equity funds, however, differ from hedge funds in terms of the manner in which contribution to the investment pool is made by the investors. Private equity investors typically commit to invest a certain amount of money with the fund over the life of the fund, and make their contributions in response to “capital calls” from the fund’s general partner. Private equity funds are long term investments, provide for liquidation at the end of the term specified in the fund’s governing documents and offer little, if any, opportunities for investors to redeem their investments. A private equity fund may distribute cash to its investors when it sells its portfolio investment, or it may distribute the securities of a portfolio company.

Venture Capital Fund

Venture capital pools are similar to hedge funds or private equity; they attract the same class of investors. Venture capital funds, however, invest in the start-up or early stages of a company. Unlike hedge fund advisors, general partners of venture capital funds often play an active role in the companies in which the funds invest. In contrast to a hedge fund, which may hold an investment in a portfolio security for an indefinite period based on market events and conditions, a venture capital fund typically seeks to liquidate its investment once the value of the company increases above the value of the investments.

Commodity Pool

Commodity pools are investment trusts, syndicates or similar enterprises that are operated for the purpose of trading commodity futures. The investment concentration in commodity futures distinguishes commodity pools from hedge funds.

DOMESTIC AND OFFSHORE HEDGE FUND

Domestic Hedge Fund

Domestic hedge funds are usually organized (in USA) as limited partnerships to accommodate investors that are subject to U.S. income taxation. The fund's sponsor typically is the general partner and investment adviser. Hedge funds may also take the form of limited liability companies (LLC) or business trusts. LLPs, LLCs and business trusts are generally not separately taxed and, as a result, income is taxed only at the level of the individual investors. Each of three firms also limits investors liability; LLCs offer the additional benefit of limited liability for fund advisors (general partners).

Offshore Hedge Fund

Offshore hedge funds are typically organized as corporations in countries such as the Cayman Islands, British Virgin Islands, the Bahamas, Panama, The Netherlands Antilles or Bermuda. Offshore funds generally attract investments of U.S. tax exempt entities, such as pension funds, charitable trusts, foundations and endowments, as well as non-U.S. residents. U.S. tax-exempt investors favour investments in offshore hedge funds because they may be subject to taxation if they invest in domestic limited partnership hedge funds.

Market Benefits of Hedge Funds

<i>A Taxonomy of Hedge Fund Strategies</i>	
<i>Strategy</i>	<i>Description</i>
Directional Trading	Based upon speculation of market direction in multiple asset classes. Both model-based systems and subjective judgment are used to make trading decisions.
Relative Value	Focus on spread relationships between pricing components of financial assets. Market risk is kept to minimum and many managers use leverage to enhance returns.
Specialist Credit	Based around lending to credit sensitive issuers. Funds in this strategy conduct a high level of due diligence in order to identify relatively inexpensive securities.
Stock Selection	Combine long and short positions, primarily in equities, in order to exploit under and overvalued securities. Market exposure can vary substantially.

Hedge funds can provide benefits to financial markets by contributing to market efficiency and enhance liquidity. Many hedge fund advisors take speculative trading positions on behalf of their managed hedge funds based extensive research about the true value or future value of a security. They may also use short term trading strategies to exploit perceived mis-pricings of securities. Because securities markets are dynamic, the result of such trading is that market prices of securities will move toward their true value. Trading on behalf of hedge funds can thus bring price information to the securities markets, which can translate into market price efficiency. Hedge funds also provide liquidity to the capital markets by participating in the market.

Hedge funds play an important role in a financial system where various risks are distributed across a variety of innovative financial instruments. They often assume risks by serving as ready counter parties to entities that wish to hedge risks. For example, hedge funds are buyers and sellers of certain derivatives, such as securitised financial instruments, that provide a mechanism for banks and other creditors to un-bundle the risks involved in real economic activity. By actively participating in the secondary market for these instruments, hedge funds can help such entities to reduce or manage their own risks because a portion of the financial risks are shifted to investors in the form of these tradable financial instruments. By reallocating financial risks, this market activity provides the added benefit of lowering the financing costs shouldered by other sectors of the economy. The absence of hedge funds from these markets could lead to fewer risk management choices and a higher cost of

capital. Hedge fund can also serve as an important risk management tool for investors by providing valuable portfolio diversification. Hedge fund strategies are typically designed to protect investment principal. Hedge funds frequently use investment instruments (e.g. derivatives) and techniques (e.g. short selling) to hedge against market risk and construct a conservative investment portfolio – one designed to preserve wealth.

In addition, hedge funds investment performance can exhibit low correlation to that of traditional investments in the equity and fixed income markets. Institutional investors have used hedge funds to diversify their investments based on this historic low correlation with overall market activity.

EXCHANGE TRADED FUNDS

Exchange traded funds (ETFs) are a new variety of mutual fund that was first introduced 1993. ETFs are sometimes described as more “tax efficient” than traditional equity mutual funds, since in recent years, some large ETFs have made smaller distributions of realized and taxable capital gains than most mutual funds.

In short, they are similar to index mutual funds but are traded more like a stock. As their name implies, Exchange Traded Funds represent a basket of securities that are traded on an exchange. Gold ETFs are most popular among other ETFs, physical gold is kept as underlying security. As with all investment products, exchange traded funds have their share of advantages and disadvantages.

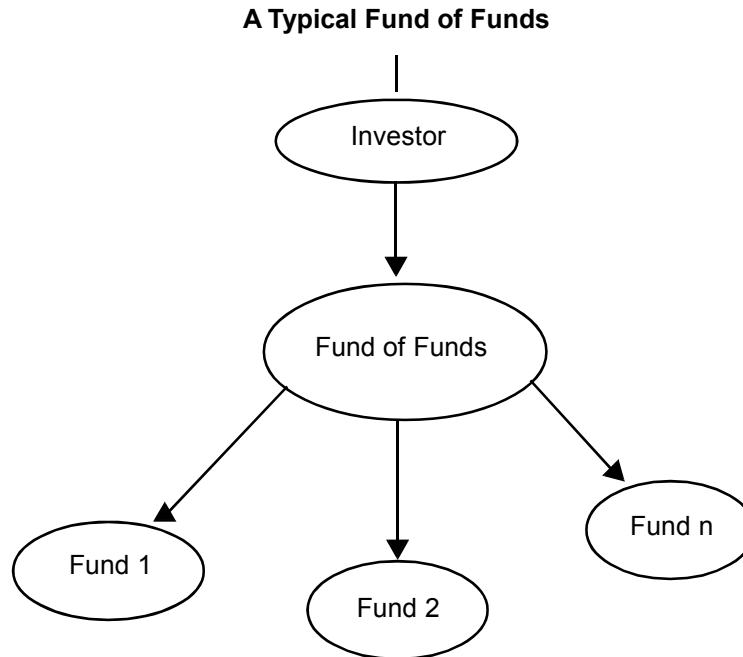
<i>Advantages of Exchange Traded Funds</i>	<i>Disadvantages of Exchange Traded Funds</i>
ETFs can be bought and sold throughout the trading day, allowing intraday trading - which is rare with mutual funds.	Commissions - like stocks, trading exchange traded funds are an extra cost.
Traders have the ability to short or buy ETFs on margin.	Only institutions and the extremely wealthy can deal directly with ETF. Companies must buy through a broker.
Low annual expenses rival the cheapest mutual funds.	Unlike mutual funds, ETFs don't necessarily trade at the net asset values of their underlying holdings, meaning an ETF could potentially trade above or below the value of the underlying portfolios.

FUND OF FUNDS (FOFS)

Fund of funds (FoFs) is a mutual fund scheme, which invests in the schemes of same mutual funds or other mutual funds, instead of investing in securities. These funds can invest in equity oriented, debt oriented and liquid schemes or sector specific schemes. Depending on the investment style of the fund managers, fund of funds schemes can be broadly classified into:

Sector specific funds: Such type of funds invest in different sectors of the economy and thus hedge themselves against the under performance of any sector by taking the advantage from the rise in another sector.

Asset allocation funds: These funds diversify investment by holding several different asset classes at the same time. By varying the stocks to bonds proportion, the fund endeavors to endow the investors, with an appropriate asset allocation in different stages of their lives. They are also known as life cycle funds.



BENEFITS OF FUND OF FUNDS SCHEME

Diversification

As a fund of funds invests in the schemes of other funds, it provides a greater degree of diversification.

Uncomplicated

Instead of investing in different stocks/units of mutual funds and keeping a track record of all of them, it will be much easier to invest in and track only one fund, which in turn invests in other mutual funds.

Cheap

While entering into the capital markets it is difficult to diversify because of limited funds. Fund of funds provide an opportunity to go for diversification with comparatively limited amounts.

Risk

Investors can trim down the risk by choosing this route. Because of diversification, even if one stock/scheme is not performing well risk level comes down.

Expertise of Various Managers

As in the case of schemes of mutual funds, fund of funds scheme also work under the due diligence of a fund manager. This gives the scheme additional expertise as compared to other mutual funds schemes. These schemes also provide access to information which may be difficult to obtain for an investor on a case by case basis.

DISADVANTAGES OF FUND OF FUNDS SCHEME

However, just like any other investment, fund of funds is not free from shortcomings. Few of the disadvantages are specified below.

Additional Fees

The more diversified the fund is, the greater the likelihood that the investor will incur an incentive fee on one or more of the constituent managers, regardless of overall FoF performance.

Associated Risks

Risks associated with all the underlying funds get added at this level. Following are the type of risks associated with fund of funds scheme.

Management Risks

Every fund manager has a particular style of diversification. This diversification style will be in perfect correlation with the number of managers involved. The views of a manager may be altogether different from the market.

Operational Risks

Due diligence of a scheme in itself gives rise to operational risks. Continuous monitoring is required for knowing about performance of the funds, any possibility of a fraud and to know about the investment style of the funds and any desirable or undesirable changes in it.

Qualitative Risks

These include risks associated with the management environment of the fund such as organizational structure, infrastructure, investment process, operational issues etc.

Regulations in India

The fund of funds scheme was introduced in the Indian market by making suitable amendments in SEBI (Mutual Funds) (Amendment) Regulations, 2003.

LESSON ROUND UP

- Instruments can be classified into three categories viz. Pure, Hybrid and Derivatives.
- Equity shares, commonly referred to as ordinary share also represents the form of fractional ownership in which a shareholder, as a fractional owner, undertakes the maximum entrepreneurial risk associated with a business venture. The holder of such shares is the member of the company and has voting rights.
- Owners of preference shares are entitled to a fixed dividend or dividend calculated at a fixed rate to be paid regularly before dividend can be paid in respect of equity shares.
- Debenture includes debenture stock, bonds and any other securities of a company, whether constituting a charge on the assets of the company or not.
- Sweat equity share is an instrument permitted to be issued by specified Indian companies, under Section 2(88) of Companies Act, 2013.
- A Tracking stock is a type of common stock that “tracks” or depends on the financial performance of a specific business unit or operating division of a company, rather than the operations of the company as a whole.
- GDR is a form of depository receipt or certificate created by the Overseas Depository Bank outside India denominated in dollar and issued to non-resident investors against the issue of ordinary shares or foreign currency convertible bonds of issuing company.
- Derivatives are contracts which derive their values from the value of one or more of other assets (known as underlying assets).
- Future is a contract to buy or sell an underlying financial instrument at a specified future date at a price when the contract is entered.

- An option contract conveys the right to buy or sell a specific security or commodity at specified price within a specified period of time.
- Private equity fund is an unregistered investment vehicle in which investors pool money to invest.

GLOSSARY

At-the-Money Option	Term used to describe an option or a warrant with an exercise price equal to the current market price of the underlying asset.
Coupon Rate	The interest rate stated on the face of coupon.
Hedge	An asset, liability or financial commitment that protects against adverse changes, in the value of or cash flows from another investment or liability. An unhedged investment or liability is called an “exposure”. A perfectly matched hedge will gain in value what the underlying expense loses or what the underlying exposure gains.
Premium	If an investor buys a security for a price above its evaluate value at a maturity he has paid a premium for it.
Forward Contract	An agreement for the future delivery of the underlying commodity or security at a specified price at the end of a designated period of time. Unlike a future contract, a forward contract is traded over the counter and its terms are negotiated individually. There is no clearing house for forward contracts, and the secondary market may be non-existent or thin.
Hypothecation	Pledging assets against a loan. The ownership of the asset or the income from the asset is not transferred, except that in default of repayment of loan the asset may be sold to realize its value. Brokers will accept shares as collateral for loans to finance purchase of shares or to cover short sales.

SELF TEST QUESTIONS

(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation.)

1. State and explain in brief about various new capital market instruments in Indian Securities Market.
2. Give a comparative view of various types of preference shares prevalent in the market.
3. Dwell upon the features and advantages of convertible debentures. Distinguish between fully and partly convertible debentures.
4. What is Exchange Traded Funds (ETFs)? Briefly discuss the advantages and disadvantages of ETFs.
5. Write short notes on –
 - (a) Sweat Equity Shares
 - (b) Mortgage Backed Securities
 - (c) Derivatives
 - (d) Pure and Hybrid Instruments
 - (e) Fund of funds scheme
6. Distinction between Domestic and offshore hedge fund?

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Lesson 3

Credit Rating & IPO Grading

LESSON OUTLINE

- Introduction
- Concept & Overview
- Purposes
- Uses of Credit Rating
- Factors for Success of a Rating System
- Important Issues in Credit Rating
- Rating Methodologies
- Rating Process
- Regulatory Framework
- SEBI (Credit Rating Agencies) Regulations, 1999
- Transparency and Disclosure Norms for CRAs
- Internal Audit of CRAs
- Rating Symbols & Definitions
- IPO Grading
- LESSON ROUND-UP
- GLOSSARY
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

Credit Rating is a symbolic indication of the current opinion regarding the relative capability of a corporate entity to service its debt obligations in time with reference to the instrument being rated. It enables the investor to differentiate between debt instruments on the basis of their underlying credit quality. In determining a rating, both qualitative and quantitative analyses are employed. The judgment is qualitative in nature and the role of the quantitative analysis is to help make the best possible overall qualitative judgment or opinion.

This lesson is designed to give a comprehensive, regulatory framework of Credit Rating Agencies (CRAs). After going through this lesson, the student will be able to understand the concept, uses, purpose, rating methodologies of CRAs, the provisions stipulated in the regulations, guideline relating to CRAs, basic understanding of IPO grading, Internal Audit of CRA by a Practicing Company Secretary etc.

INTRODUCTION

Credit rating, in general sense, is the evaluation of the credit worthiness of an individual or of a business concern or of an instrument of a business based on relevant factors indicating ability and willingness to pay obligations as well as net worth.

'Encyclopedia of Banking & Finance' by Charles J. Woelfel states that a credit rating is a letter or number used by a mercantile or other agency in reports and credit rating books to denote the ability and disposition of various businesses (individual, proprietorship, partnership or corporation) to meet their financial obligations. It also states that ratings are used as a guide to the investment quality of bonds and stocks, based on security of principal and interest (or dividends), earning power, mortgage position, market history and marketability.

Credit ratings establish a link between risk and return. An investor or any other interested person uses the rating to assess the risk-level and compares the offered rate of return with his expected rate of return.

EVOLUTION OF CREDIT RATING

The first Mercantile Credit Agency was established in New York in 1841. Its first rating guide was published in 1859 by Robert Dun. Another similar agency was set up by John Bradstreet which published its rating guide in 1857. These two agencies were merged to form Dun and Bradstreet in 1933 which acquired Moody's Investor Service in 1962. Moody's was founded by Moody in 1900. The other world renowned rating agency namely Standard and Poor was created in 1941 by merging the Standard Statistics Company and Poor's Publishing Company which had their origin earlier.

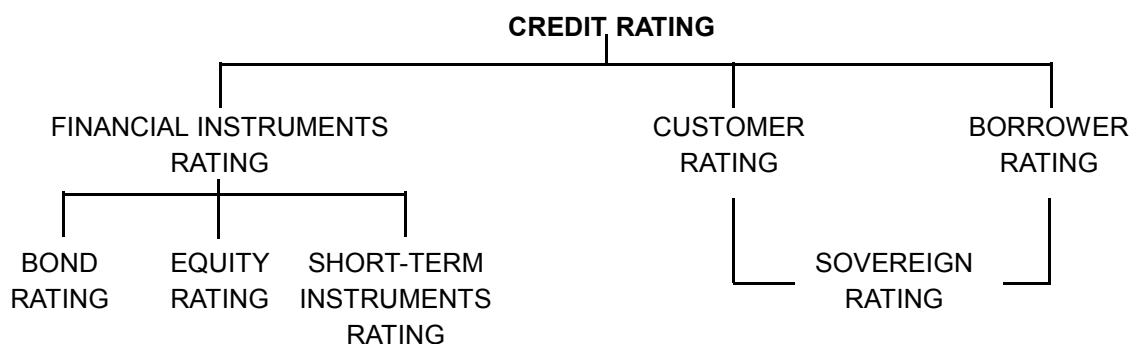
In India CRISIL (Credit Rating and Information Services (India) Limited) was set up as the first credit rating agency in 1987. This was followed by ICRA Limited (Investment Information and Credit Rating Agency of India Limited) in 1991 and CARE (Credit Analyses and Research Limited) in 1994 and then in 1999 Fitch Rating India Pvt. Ltd. now known as India Ratings and Research Pvt. Ltd., Brickwork Rating Pvt. Ltd. in 2008, SMERA (SME Rating Agency of India Limited) in 2011 and Info Merics Valuation and Ratings Pvt. Ltd. All these seven credit rating agencies are registered with the SEBI.

CONCEPT & OVERVIEW

Credit Rating is a symbolic indication of the current opinion regarding the relative capability of a corporate entity to service its debt obligations in time with reference to the instrument being rated. It enables the investor to differentiate between debt instruments on the basis of their underlying credit quality. To facilitate simple and easy understanding, credit rating is expressed in alphabetical or alphanumerical symbols.

A rating is specific to a debt instrument and is intended to grade different such instruments in terms of credit risk and ability of the company to service the debt obligations as per terms of contract namely - principal as well as interest. A rating is neither a general purpose evaluation of a corporate entity, nor an over all assessment of the credit risk likely to be involved in all the debts contracted or to be contracted by such entity.

Though credit rating is considered more relevant for gradation of debt securities, it can be applied for other purposes also. The diagram below depicts various types of credit ratings:



PURPOSES

The various instruments which can be rated may be –

- Credit rating does not bound the investor to decide whether to hold or sell an instrument as it does not take into consideration factors such as market prices, personal risk preferences and other consideration which may influence an investment decision. It does not create any fiduciary relationship between the rating agency and the user of the rating. A credit rating agency does not perform an audit but relies on information provided by the issuer and collected by the analysts from different sources hence it does not guarantee the completeness or accuracy of the information on which the rating is based.
- Long-term/Medium-term debt obligations such as debentures, bonds, preference shares or project finance debts are considered long-term and debts ranging from 1 to 3 years like fixed deposits are considered medium-term;
- Short-term debt obligations - the period involved is one year or less and cover money market instruments such as commercial paper, credit notes, cash certificates etc.;
- Equity Grading and Assessment, structured obligations, municipal bonds, mutual fund schemes, plantation schemes, real estate projects, infrastructure related debts, ADR, GDR issues, bank securities etc.

In determining a rating, both qualitative and quantitative analyses are employed. The judgment is qualitative in nature and the role of the quantitative analysis is to help make the best possible overall qualitative judgment or opinion. The reliability of the rating depends on the validity of the criteria and the quality of analysis.

The quality of credit rating mainly depends upon the quality of the rating agency and rating elements also. The agency should have good reputation, personal competence, independence, qualified and experienced staff.

USES OF CREDIT RATING

Credit rating is extremely important as it not only plays a role in investor protection but also benefits industry as a whole in terms of direct mobilization of savings from individuals. Rating also provide a marketing tool to the company and its investment bankers in placing company's debt obligations with a investor base that is aware of, and comfortable with, the level of risk. Ratings also encourage discipline amongst corporate borrowers to improve their financial structure and operating risks to obtain a better rating for their debt obligations and thereby lower the cost of borrowing. Companies those get a lower rating are forewarned, as it were and have the freedom, if they desire, to take steps on their financial or business risks and thereby improve their standing in the market.

Credit rating is useful to investors, issuers, intermediaries and regulators.

For Investors

The main purpose of credit rating is to communicate to the investors the relative ranking of the default loss probability for a given fixed income investment, in comparison with other rated instruments. In a way it is essentially an information service. In the absence of professional credit rating, the investor has to largely depend on his familiarity with the names of promoters or collaborators of a company issuing debt instruments. This is not a reliable method. Credit rating by skilled, competent and credible professionals eliminates or at least minimizes the role of name recognition and replaces it with a well researched and properly analyzed opinion. This method provides a low cost supplement to investors. Large investors use information provided by rating agencies such as upgrades and downgrades and alter their portfolio mix by operating in the secondary market. Investors also use the industry reports, corporate reports, seminars and open access provided by the credit rating agencies.

For Issuers

The market places immense faith in opinion of credit rating agencies, hence the issuers also depend on their critical analysis. This enables the issuers of highly rated instruments to access the market even during adverse market conditions. Credit rating provides a basis for determining the additional return (over and above a risk free return) which investors must get in order to be compensated for the additional risk that they bear. The difference in price leads to significant cost savings in the case of highly rated instruments.

For Intermediaries

Rating is useful to Intermediaries such as merchant bankers for planning, pricing, underwriting and placement of the issues. Intermediaries like brokers and dealers in securities use rating as an input for monitoring risk exposures. Merchant bankers also use credit rating for pre-packaging issues by way of asset securitization/ structured obligations.

For Regulators

The Reserve Bank of India (RBI) prescribes a number of regulatory uses of ratings. The RBI requires that a NBFC must have minimum investment grade credit rating if it intends to accept public deposits. As per money market regulations of the RBI, a corporate must get an issue of CP rated and can issue such paper subject to a minimum rating. SEBI has also stipulated that ratings are compulsory for all public issue of debentures. SEBI has also made mandatory for acceptance of public deposit by Collective Investment Schemes.

FACTORS FOR SUCCESS OF A RATING SYSTEM

- Credible and independent structure and procedures;
- Objectivity and impartiality of opinions;
- Analytical research, integrity and consistency;
- Professionalism and industry related expertise;
- Confidentiality;
- Timeliness of rating review and announcement of changes;

Ability to reach wide range of investors by means of press reports, print or electronic media and investor oriented research services.

IMPORTANT ISSUES IN CREDIT RATING***Investments and Speculative Grades***

Debt instrument rated 'BBB' & above are classified as investment grade ratings. Instruments that are rated 'BB' and below are classified as speculative grade ratings. Rating agencies do not recommend or indicate the rating levels of instruments up to which one should or should not invest.

Surveillance

The rating published by credit rating agencies is subjected to a continuous surveillance during the life of the instrument or so long as any amount is outstanding against the specific instrument. The frequency of surveillance may range between quarterly or yearly. A formal and extensive written review is taken at least once in a year but where some specific concern arises about the industry or the issuing entity, the review is taken up immediately. Where the rating agency justified may change the rating by upgradation or downgradation depending on the likely impact of changing circumstances on the debt servicing capability of the issuer. In other cases, the rating is retained at the same level.

Credit Watch

When a major deviation from the expected trends of the issuers business occurs, or when an event has taken

place, it creates an impact on the debt servicing capability of the issuer and warrants a rating change, the rating agency may put such ratings under credit watch till the exact impact of such unanticipated development is analyzed and decision is taken regarding the rating change. The credit watch listing may also specify positive or negative outlooks. It should be noted that being under credit watch does not necessarily mean that there would be a rating change.

Ownership as a rating consideration

Ownership by a strong concern may enhance the credit rating of an entity, unless there exists a strong barrier separating the activities of the parent and the subsidiary. The important issues involved in deciding the relationship are - the mutual dependence on each other, legal relationship, to what extent one entity has the desire and ability to influence the business of the other, and how important is the operation of the subsidiary to the owner.

Rating agency keeps the information provided by the issuer confidential and completes the rating within 2 to 4 weeks. Once the rating is assigned, it is communicated to the issuer, who is given an opportunity to make one request for a review, only in case fresh facts or clarifications become relevant. After these are considered, the final rating is assigned. In India, the issuer has the option of not accepting the assigned rate in which case the rating is not disclosed by the rating agency. However, if the rating is accepted, it comes under the surveillance process of the concerned agency.

RATING METHODOLOGIES

RATING OF MANUFACTURING COMPANIES

The factors generally considered for rating of manufacturing companies are as under:

Industry Risk

It is defined as the strength of the industry within the economy and relativity to the economic trends. It is evaluated on the basis of factors like business cyclicity, earnings volatility, growth prospects, demand - supply projections, entry barriers and extent of competition and nature and extent of regulation.

Company's industry and market position

The company's sales position in its major fields and its historical background of its market position is analyzed along with ability to sustain/increase market shares; brand strengths and position; price leadership and distribution and marketing strengths/weaknesses.

Operating efficiencies

Ability to control costs, productivity efficiencies relative to others, labour relationship, extent of forward and backward integration, access to raw materials/markets, and technology.

Accounting Quality

Financial statements are adjusted for non-standard accounting treatments. Overall evaluation of the accounting policies employed and the extent to which they understate or overstate financial performance and position. These include analysis of auditor's qualifications, revenue recognition, depreciation policy, inventory evaluation, funding for pension liabilities, undervalued assets etc.

Financial flexibility

Evaluation of the company's financing needs, plans and alternatives, its flexibility to accomplish its financing programmes under stress without damaging creditworthiness.

Earnings protection

The key measurements which indicate the basic long term earnings power of the company including return on

capital, profit margins, earnings from various business segments, sources of future earnings growth, coverage ratios etc.

Financial leverage

Relative usage of debt and levels of debt appropriate to different types of businesses, utilization of long and short term sources of funds, management of working capital.

Cash flow adequacy

It is the relationship of cash flows to leverage and the ability to internally meet all cash needs of the business. It measures the magnitude and variability of future cash flows relative to debt servicing obligations and other commitments such as group company funding, BIFR packages and contingent liabilities. This analysis goes into the inherent protective factors for expected cash flows of the company and the sensitivity of these cash flows to changes in variables like raw material costs and selling prices.

Management evaluation

The record of achievement in operations and financial results, strategic and financial planning, commitment, consistency and credibility, overall quality of management, line of succession, strength of middle management and organization structure and its linkage with the operating environment and management strategies.

RATING OF FINANCIAL SERVICES COMPANIES

The rating methodology for non-banking financial services companies is based on CAMELS model encompassing, Capital adequacy, Asset quality, Management, Earnings, Liquidity, systems and control.

In 1995, RBI had set up a working group under the chairmanship of Shri S. Padmanabhan to review the banking supervision system. The Committee made certain recommendations and based on such suggestions a rating system for domestic and foreign banks based on the international CAMELS model combining financial management and systems and control elements was introduced for the inspection cycle commencing from July 1998. It recommended that the banks should be rated on the lines of international CAMELS model. The following six parameters are recommended:

- (i) *Capital Adequacy* : Capital adequacy is measured by the ratio of capital to risk-weighted assets (CRAR). A sound capital base strengthens confidence of depositors.
- (ii) *Asset Quality* : One of the indicators for asset quality is the ratio of non-performing loans to total loans (GNPA). The gross non-performing loans to gross advances ratio is more indicative of the quality of credit decisions made by bankers. Higher GNPA is indicative of poor credit decision-making.
- (iii) *Management* : The ratio of non-interest expenditures to total assets (MGNT) can be one of the measures to assess the working of the management. This variable, which includes a variety of expenses, such as payroll, workers compensation and training investment, reflects the management policy stance.
- (iv) *Earnings* : It can be measured as the return on asset ratio.
- (v) *Liquidity* : Cash maintained by the banks and balances with central bank, to total asset ratio (LQD) is an indicator of bank's liquidity. In general, banks with a larger volume of liquid assets are perceived safe, since these assets would allow banks to meet unexpected withdrawals.
- (iv) *Systems and Control* : The internal controls, other systems and procedures of banks are considered.

RATING OF STRUCTURED OBLIGATIONS/ASSET SECURITISATION

Structured borrowing arrangements are entered into by companies for various reasons. However, the most important one is that less credit worthy instruments or corporates are able to tap sources of funds at a more advantageous borrowing rate by offering a variety of credit enhancements.

The process of converting loans or receivables into negotiable instruments is known as securitization. These negotiable instruments are sold to investors; they are secured by the underlying assets and have other credit enhancements. Securitization transforms illiquid assets like the renewable portfolio on the balance sheet of a lender into a marketable security.

The principal credit risk in asset backed financing is potential impairment of cash flows due to the assets becoming defaulting on repayments or turning into a loss. The main factors considered for credit rating are the overall risk profile and monitoring and collection procedures of the issuer; the quality of the assets being securitized; the process of selection of the asset pool to be securitized; the characteristics of the pool and the cash flows from it based on the past record of its behaviour. The possible credit loss and other deficiencies of the pool in terms of timing and quantum of cash flows are analyzed and the extent and nature of credit enhancement is then determined.

Other important considerations in a securitization transaction are the legal and tax structure and the ability and willingness of the services and trustee to manage and maintain control on assets and payment streams from them.

RATING PROCESS

Rating process refers to the typical practices and procedures which a rating agency follows to gather information for evaluating the credit risk of specific issuers and issues, to analyze and conclude on the appropriate rating to monitor the credit quality of the rated issuer or security over time, deciding on timely changes in ratings, as and when companies' fundamentals change and to keep investors and the market players informed. All these are interrelated and on going processes. The rating agencies in India have adopted the methodology of the major international credit rating agencies.

The rating process begins with the receipt of a mandate from the issuer company. The next step is to form analytical teams with sectoral skills.

Information gathering/analysis

For the basic research, obtain credit related data, both statistical and qualitative, from a multitude of sources like annual reports, prospectus, industry/sectoral economic data, government reports, news reports, discussions with industry/ regulatory/other circles. Statistical data bases are developed over time to enable comparability across major issuer categories.

Meetings with Management

Meetings are held with key operating personnel of the company covering broadly the background, history, organisational structure, operating performance, financial management and topics of special relevance to the company's future. The central focus of all discussions is the same with analysts looking for information that will help them to understand the issuer's ability to generate cash from operations to meet debt obligations over the next several years. It is the management's opportunity to explain the company's business and financial strategies. Finally, a meeting with top management is held, where apart from corporate strategy and philosophy, key issues relevant to the rating are discussed. A plant visit with the major manufacturing/work centres and project sites is invariably undertaken.

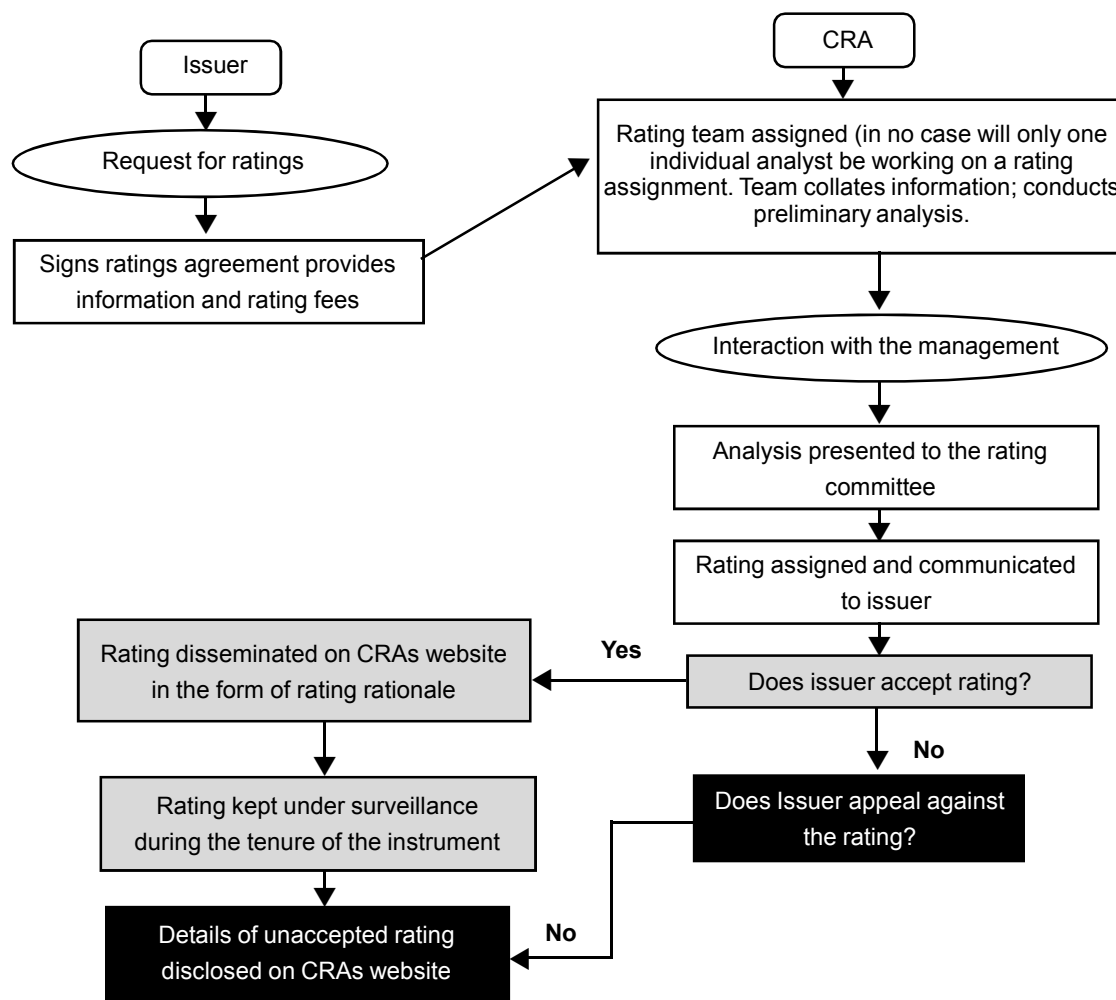
In India, credit rating agencies do not undertake unsolicited ratings merely based on published information of the company. The quality of credit rating will greatly improve with privileged information obtained from the companies by credit rating agencies. It is possible to have two agencies to do the rating for a particular issue and the findings may even vary, because rating is a matter of perceptions. But generally the findings will not be varying widely.

The ratings can be published by the agency only after approval and with the permission of the issuer. Subsequent changes emerging out of the monitoring by the credit rating agency will be published even if such changes are not found acceptable to the issuers. The issuer may appeal on the findings of an agency. In such a case the

agency will undertake a review and thereafter indicate its final decision. Unless the rating agency has overlooked critical information at the first stage, chances of the rating being changed on appeal will be rare.

There is no system yet to rate the rating agency. Informed public opinion is the touch stone on which the rating companies are being assessed. The success of a rating agency is measured by the quality, consistency and integrity and the record of acceptance in the market. The rating is always about a particular issue and not generally about the issuer.

Rating Process



REGULATORY FRAMEWORK

SEBI (CREDIT RATING AGENCIES) REGULATIONS, 1999

SEBI regulations for Credit Rating Agencies (CRAs) cover rating of securities only and not rating of fixed deposits, foreign exchange, country ratings, real estates etc. CRAs can be promoted by public financial institutions, scheduled commercial banks, foreign banks operating in India, foreign credit rating agencies recognised in the country of their incorporation, having at least five years experience in rating, or any company or a body corporate having continuous net worth of minimum ₹100 crore for the previous five years. CRAs would be required to have a minimum net worth of ₹ 5 crore. A CRA can not rate a security issued by its promoter. No Chairman, Director or Employee of the promoters shall be Chairman, Director or Employee of CRA or its rating committee. A CRA can not rate securities issued by any borrower, subsidiary, an associate promoter of CRA, if there are common Chairman, Directors and Employees between the CRA or its rating committee and these entities. A CRA can not

rate a security issued by its associate or subsidiary if the CRA or its rating committee has a Chairman, Director or Employee who is also a Chairman, Director or Employee of any such entity. CRAs would have to carry out periodic reviews of the ratings given during the lifetime of the rated instrument. For ensuring that corporates provide correct/ adequate information to CRAs, a clause would be incorporated in the listing agreement of the stock exchanges requiring the companies to co-operate with the rating agencies in giving correct and adequate information. Issuers coming out with a public/rights issue of debt securities would be required to incorporate an undertaking in the offer documents promising necessary co-operation with the rating agency in providing true and adequate information.

Registration of Credit Rating Agencies

Any person proposing to commence any activity as a credit rating agency should make an application to SEBI for the grant of a certificate of initial registration for the purpose. An application for the grant of a certificate should be made to SEBI accompanied by a non-refundable specified application fee.

Promoter of Credit Rating Agency

SEBI should not consider an application unless the applicant is promoted by a person belonging to any of the following categories, namely:

- (i) a public financial institution;
- (ii) a scheduled commercial bank;
- (iii) a foreign bank operating in India with the approval of the Reserve Bank of India;
- (iv) a foreign credit rating agency recognized under Indian Law and having at least five years experience in rating securities;
- (v) any company or a body corporate, having continuous net worth of minimum rupees one hundred crores as per its audited annual accounts for the previous five years in relation to the date on which application to SEBI is made seeking registration.

Eligibility Criteria

SEBI shall not consider an application for the grant of a certificate unless the applicant satisfies the following conditions, namely:

- (a) the applicant is set up and registered as a company under the Companies Act, 2013;
- (b) the applicant has, in its Memorandum of Association, specified rating activity as one of its main objects;
- (c) the applicant has a minimum net worth of ₹ 5 crores;
- (d) the applicant has adequate infrastructure, to enable it to provide rating services;
- (e) the applicant and the promoters of the applicant, have professional competence, financial soundness and general reputation of fairness and integrity in business transactions, to the satisfaction of SEBI;
- (f) neither the applicant, nor its promoter, nor any director of the applicant or its promoter, is involved in any legal proceeding connected with the securities market, which may have an adverse impact on the interests of the investors;
- (g) neither the applicant, nor its promoters, nor any director, of its promoter has at any time in the past been convicted of any offence involving moral turpitude or any economic offence;
- (h) the applicant has, in its employment, persons having adequate professional and other relevant experience to the satisfaction of the SEBI;

- (i) neither the applicant, nor any person directly or indirectly connected with the applicant has in the past been –
 - (i) refused by SEBI a certificate under these regulations or
 - (ii) subjected to any proceedings for a contravention of the Act or of any rules or regulations made under the Act.
- (j) the applicant, in all other respects, is a fit and proper person for the grant of a certificate;
- (k) grant of certificate to the applicant is in the interest of investors and the securities market.

Application to Confirm to the Requirements

Any application for a certificate, which is not complete in all respects or does not confirm to the requirement or instructions as specified should be rejected by SEBI. However before rejecting any application, the applicant should be given an opportunity to remove, within thirty days of the date of receipt of relevant communication, from SEBI such objections as may be indicated by SEBI. It has been further provided that SEBI may on sufficient reason being shown, extend the time for removal of objections by such further time, not exceeding thirty days to enable the applicant to remove such objections.

Furnishing of Information, Clarification and Personal Representation

SEBI may require the applicant to furnish such further information or clarification as it consider necessary, for the purpose of processing of the application. SEBI if so desires, may ask the applicant or its authorised representative to appear before SEBI for personal representation in connection with the grant of a certificate.

Grant of Certificate

SEBI grants a certificate of registration after getting satisfied that the applicant is eligible for the grant of a certificate of registration. The certificate of registration granted under these regulation shall be valid unless it is suspended or cancelled by SEBI. The credit rating agency who has already been granted certificate of registration by SEBI, prior to the commencement of the SEBI (Change in Conditions of Registration of Certain Intermediaries) Regulations, 2016 shall be deemed to have been granted a certificate of registration, in terms of these regulations. The grant of certificate of registration should be subject to the payment of the specified registration fee in the manner prescribed.

Conditions of Certificate

The certificate granted is subject to the condition that the credit rating agency should comply with the provisions of the Act, the regulations made thereunder and the guidelines, directives, circulars and instructions issued by SEBI from time to time on the subject of credit rating. The credit rating agency should forthwith inform SEBI in writing where any information or particulars furnished to SEBI by a credit rating agency is found to be false or misleading in any material particular; or has undergone change subsequently to its furnishing at the time of the application for a certificate. Where the credit rating agency proposes change in control, it shall obtain prior approval of SEBI for continuing to act as such after the change.

Procedure where Certificate is not granted

SEBI may reject the application if after considering an application is of the opinion that a certificate should not be granted, after giving the applicant a reasonable opportunity of being heard. The decision of SEBI not to grant the certificate should be communicated by SEBI to the applicant within a period of thirty days of such decision, stating the grounds of the decision. Any applicant aggrieved by the decision of SEBI rejecting his application may, within a period of thirty days from the date of receipt by him of the communication apply to SEBI in writing for re-consideration of such decision. Where an application for re-consideration is made, SEBI should consider the application and communicate to the applicant its decision in writing, as soon as may be.

Guidelines for Credit Rating Agencies (CRAs)

SEBI constituted a committee on “Strengthening the Guidelines and Raising Industry Standards for Credit Rating Agencies (CRAs)”, which included representatives from all the CRAs. The objective of the Committee was to deliberate upon measures and guidelines to bring about greater transparency in the policies of the CRAs, enhance the standards followed by the industry and, thereby, facilitate ease of understanding of the ratings by the investors.

These guidelines cover the following broad areas:

- I. Formulation of Rating Criteria and rating processes and public disclosure of the same.
- II. Accountability of Rating Analysts
- III. Standardisation of Press Release for rating actions.
- IV. Functioning and evaluation of Rating Committees/Sub-Committees.
- V. Disclosure of ratings in case of non-acceptance by an issuer
- VI. Disclosure in case of delay in periodic review of ratings.
- VII. Policy in respect of non-cooperation by the issuer.
- VIII. Strengthening and enhancing the relevance of Internal Audit of CRAs, viz. appointment and rotation of auditors and scope of the audit.

Code of Conduct

Every credit rating agency is required to abide by the Code of Conduct as per SEBI Regulations:

1. A credit rating agency shall make all efforts to protect the interests of investors.
2. A credit rating agency, in the conduct of its business, shall observe high standards of integrity, dignity and fairness in the conduct of its business.
3. A credit rating agency shall fulfill its obligations in a prompt, ethical and professional manner.
4. A credit rating agency shall at all times exercise due diligence, ensure proper care and exercise independent professional judgment in order to achieve and maintain objectivity and independence in the rating process.
5. A credit rating agency shall have a reasonable and adequate basis for performing rating evaluations, with the support of appropriate and in depth rating researches. It shall also maintain records to support its decisions.
6. A credit rating agency shall have in place a rating process that reflects consistent and international rating standards.
7. A credit rating agency shall not indulge in any unfair competition nor shall it wean away the clients of any other rating agency on assurance of higher rating.
8. A credit rating agency shall keep track of all important changes relating to the client companies and shall develop efficient and responsive systems to yield timely and accurate ratings. Further a credit rating agency shall also monitor closely all relevant factors that might affect the creditworthiness of the issuers.
9. A credit rating agency shall disclose its rating methodology to clients, users and the public.
10. A credit rating agency shall, wherever necessary, disclose to the clients, possible sources of conflict of duties and interests, which could impair its ability to make fair, objective and unbiased ratings. Further it

shall ensure that no conflict of interest exists between any member of its rating committee participating in the rating analysis, and that of its client.

11. A credit rating agency shall not make any exaggerated statement, whether oral or written, to the client either about its qualification or its capability to render certain services or its achievements with regard to the services rendered to other clients.
12. A credit rating agency shall not make any untrue statement, suppress any material fact or make any misrepresentation in any documents, reports, papers or information furnished to SEBI, stock exchange or public at large.
13. A credit rating agency shall ensure that SEBI is promptly informed about any action, legal proceedings etc., initiated against it alleging any material breach or non-compliance by it, of any law, rules, regulations and directions of SEBI or of any other regulatory body.
14. A credit rating agency shall maintain an appropriate level of knowledge and competence and abide by the provisions of the Act, regulations and circulars, which may be applicable and relevant to the activities carried on by the credit rating agency. The credit rating agency shall also comply with award of the Ombudsman passed under SEBI (Ombudsman) Regulations, 2003.
15. A credit rating agency shall ensure that there is no misuse of any privileged information including prior knowledge of rating decisions or changes.
16. (a) A credit rating agency or any of his employees shall not render, directly or indirectly any investment advice about any security in the publicly accessible media.
(b) A credit rating agency shall not offer fee-based services to the rated entities, beyond credit ratings and research.
17. A credit rating agency shall ensure that any change in registration status/any penal action taken by SEBI or any material change in financials which may adversely affect the interests of clients/investors is promptly informed to the clients and any business remaining outstanding is transferred to another registered person in accordance with any instructions of the affected clients/investors.
18. A credit rating agency shall maintain an arm's length relationship between its credit rating activity and any other activity.
19. A credit rating agency shall develop its own internal code of conduct for governing its internal operations and laying down its standards of appropriate conduct for its employees and officers in the carrying out of their duties within the credit rating agency and as a part of the industry. Such a code may extend to the maintenance of professional excellence and standards, integrity, confidentiality, objectivity, avoidance of conflict of interests, disclosure of shareholdings and interests, etc. Such a code shall also provide for procedures and guidelines in relation to the establishment and conduct of rating committees and duties of the officers and employees serving on such committees.
20. A credit rating agency shall provide adequate freedom and powers to its compliance officer for the effective discharge of his duties.
21. A credit rating agency shall ensure that the senior management, particularly decision makers have access to all relevant information about the business on a timely basis.
22. A credit rating agency shall ensure that good corporate policies and corporate governance are in place.
23. A credit rating agency shall not, generally and particularly in respect of issue of securities rated by it, be party to or instrumental for –
(a) creation of false market;

- (b) price rigging or manipulation; or
- (c) dissemination of any unpublished price sensitive information in respect of securities which are listed and proposed to be listed in any stock exchange, unless required, as part of rationale for the rating accorded.

Agreement with the Client

Every credit rating agency is required to enter into a written agreement with each client whose securities it proposes to rate, and every such agreement should include the following provisions, namely:

- (a) the rights and liabilities of each party in respect of the rating of securities shall be defined;
- (b) the fee to be charged by the credit rating agency shall be specified;
- (c) the client shall agree to a periodic review of the rating by the credit rating agency during the tenure of the rated instrument and to co-operate with the credit rating agency in order to enable the latter to arrive at, and maintain, a true and accurate rating of the clients' securities and shall in particular provide to the latter, true, adequate and timely information for the purpose;
- (d) the credit rating agency shall disclose to the client the rating assigned to the securities of the latter through regular methods of dissemination, irrespective of whether the rating is or is not accepted by the client;
- (e) the client shall agree to disclose the rating assigned to the client's listed securities by any credit rating agency during the last three years and any rating given in respect of the client's securities by any other credit rating agency, which has not been accepted by the client in the offer document;
- (f) the client shall agree to obtain a rating for any issue of debt securities in accordance with the relevant regulations.

SEBI advised the CRAs to refrain from giving Indicative Ratings without having a written agreement in place. In case such Indicative Ratings are provided by the CRA, it shall be considered as aiding and abetting the Issuer in suppression of material information by the CRA which would be in contravention of Clause 12 of Code of Conduct of CRAs and may result in violation of the provisions of section 12A of the Securities and Exchange Board of India Act, 1992 and SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 2003 by the CRA.

Monitoring of Ratings

Credit rating agency should during the lifetime of securities rated by it continuously monitor the rating of such securities. It should also disseminate information regarding newly assigned ratings, and changes in earlier rating promptly through press releases and websites, and, in the case of securities issued by listed companies, such information should also be provided simultaneously to the concerned to all the stock exchanges where the said securities are listed.

Procedure for Review of Rating

Every credit rating agency should carry out periodic review of all published ratings during the lifetime of the securities. If the client does not co-operate with the credit rating agency so as to enable the credit rating agency to comply with its obligations, the credit rating agency should carry out the review on the basis of the best available information.

However, it has been provided that if owing to such lack of co-operation, a rating has been based on the best available information, the credit rating agency should disclose to the investors the fact that the rating is so based. A credit rating agency should not withdraw a rating so long as the obligations under the security rated by it are outstanding, except where the company whose security is rated is wound up or merged or amalgamated with another company.

Dissemination of information on ratings through Press Releases

In order to enable CRAs to disseminate information on ratings promptly through press releases as per requirements of Monitoring of Ratings and Procedure for Review of Rating under SEBI (CRA) Regulations, following is clarified:

I. Initial Rating:

Scenario	Timelines – immediately but not later than
Acceptance of Rating/ Appeal for Review of Rating by the Issuer	5 working days of communication of rating by the CRA to the Issuer
Disclosure of rating as Non-Accepted Rating	In case rating is not accepted by the Issuer within a month of communication of rating by the CRA to the Issuer, the same shall be disclosed as Non-Accepted Rating on the CRA's website
Dissemination of Press Release on CRA's website and intimation of same to Stock Exchange/Debenture Trustee	2 working days of acceptance of Rating by the Issuer

II. Periodic Surveillance:

Dissemination of Press Release immediately but not later than 5 working days of Rating Committee Meeting on CRA's website and intimation of same to Stock Exchange/ Debenture Trustee.

III. Dissemination of Press Release on CRA's website and intimation of same to Stock Exchange/ Debenture Trustee in case of event based review:

Scenario	Timelines – immediately but not later than
Intimation from Issuer/ Debenture Trustee/ Bankers of the Issuer regarding delay in servicing debt obligation	2 working days of intimation
Material Events requiring review (as stated in point 1B)	7 working days of occurrence of the event

Internal Procedures to be Framed

Credit rating agency should frame appropriate procedures and systems for monitoring the trading of securities by its employees in the securities of its clients, in order to prevent contravention of SEBI (Insider Trading) Regulations, 2015; SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to the Securities Market) Regulations, 2003; and other laws relevant to trading of securities.

Disclosure of Rating Definitions

Credit rating agency should make public the definitions of the concerned rating, along with the symbol and state that the ratings do not constitute recommendations to buy, hold or sell any securities. It should also make available to the general public information relating to the rationale of the ratings, which shall cover an analysis of the various factors justifying a favourable assessment, as well as factors constituting a risk.

It is further clarified by SEBI that if the issuer does not share information sought by the CRA within 7 days of seeking such information from the Issuer, even after repeated reminders (within these 7 days) from the CRA, the CRA shall take appropriate rating action depending upon the severity of information risk of the issuer.

Submission of Information

In case any information is called by SEBI from a credit rating agency including any report relating to its activities, the credit rating agency is required to furnish such information to SEBI within a period specified or if no such period is specified, then within a reasonable time. It should also furnish to SEBI, copies of its balance sheet and profit and loss account at the close of each accounting period,

Every credit rating agency is required to comply with such guidelines, directives, circulars and instructions as issued by SEBI from time to time.

Appointment of Compliance Officer

It is under an obligation to appoint a compliance officer who will be responsible for monitoring the compliance of the Act, Rules and Regulations, notifications, guidelines, instructions etc issued by SEBI or the Central Government. The compliance officer should immediately and independently report to SEBI any non-compliance observed by him.

Maintenance of Books of Accounts, Records, etc.

Credit rating agency should keep and maintain, for a minimum period of five years, the following books of accounts, records and documents, namely:

- (i) copy of its balance sheet, as on the end of each accounting period;
- (ii) a copy of its profit and loss account for each accounting period;
- (iii) a copy of the auditor's report on its accounts for each accounting period.
- (iv) a copy of the agreement entered into, with each client;
- (v) information supplied by each of the clients;
- (vi) correspondence with each client;
- (vii) ratings assigned to various securities including upgradation and down gradation (if any) of the ratings so assigned;
- (viii) rating notes considered by the rating committee;
- (ix) record of decisions of the rating committee;
- (x) letter assigning rating;
- (xi) particulars of fees charged for rating and such other records as SEBI may specify from time to time.

Credit rating agency is required to intimate to SEBI, the place where the books of account, records and documents required to be maintained under these regulations are being maintained.

Steps on Auditor's Report

Credit rating agency should within two month's from the date of the auditor's report, take steps to rectify the deficiencies if any, made out in the auditor's report, in so far as they relate to the activity of rating of securities.

Confidentiality

Every credit rating agency shall treat, as confidential, information supplied to it by the client and no credit rating agency shall disclose the same to any other person, except where such disclosure is required under any law.

Rating Process

Credit rating agency should specify the rating process and file a copy of the same with SEBI for record and also

file with SEBI any modifications or additions made therein from time to time. It should in all cases follow a proper rating process. Credit rating agency is required to have professional rating committees, comprising members who are adequately qualified and knowledgeable to assign a rating. All rating decisions, including the decisions regarding changes in rating, should be taken by the rating committee. Credit rating agency should be staffed by analysts qualified to carry out a rating assignment. Credit rating agency should inform SEBI about new rating instruments or symbols introduced by it. Credit rating agency, while rating a security should exercise due diligence in order to ensure that the rating given by the credit rating agency is fair and appropriate. A credit rating agency should not rate securities issued by it. Rating definition, as well as the structure for a particular rating product, should not be changed by a credit rating agency, without prior information to SEBI. A credit rating agency should disclose to the concerned stock exchange through press release and websites for general investors, the rating assigned to the securities of a client, after periodic review, including changes in rating, if any.

Restrictions on Rating of Securities Issued by Promoter and Certain Entities, Connected with A Promoter, or Rating Agency

Credit rating agency shall not rate a security issued by its promoter. In case promoter is a Lending institution, its chairman, director or employee shall not be a chairman, director or employee of credit rating agency or its rating committee. No credit rating agency should rate a security issued by an entity, which is a borrower of its promoter or a subsidiary of its promoter or an associate of its promoter, if there are common Chairman, Directors between credit rating agency and these entities, there are common employees, there are common Chairman, Directors, Employees on the rating committee. No credit rating agency should rate a security issued by its associate or subsidiary, if the credit rating agency or its rating committee has a Chairman, director or employee who is also a Chairman, director or employee of any such entity. However, the Credit Rating Agency may, rate a security issued by its associate having a common independent director with it or rating committee if, –

- (i) such an independent director does not participate in the discussion on rating decisions, and
- (ii) the Credit Rating Agency makes a disclosure in the rating announcement of such associate (about the existence of common independent director) on its Board or of its rating committee, and that the common independent director did not participate in the rating process or in the meeting of its Board of Directors or in the meeting of the rating committee, when the securities rating of such associate was discussed.

Securities already rated

The above mentioned conditions do not apply to securities whose rating has been already done by a credit rating agency before the commencement of these regulations, and such securities may, subject to the provisions of the other Chapters of these regulations, continue to be rated, without the need to comply with the restrictions imposed by the regulations contained in this chapter.

Procedure for Inspection and Investigation

SEBI can appoint one or more persons as inspecting officers, to undertake inspection or investigation of the books of account, records and documents of the credit rating agencies, for any of the purposes specified in the regulations. The purposes referred to in regulation should be to ascertain whether the books of account, records and documents are being maintained properly, to ascertain whether the provisions of the Act and these regulations are being complied with, to investigate into complaints received from investors, clients or any other person on any matter having a bearing on activities of the credit rating agency and in the interest of the securities market or in the interest of investors. The inspections ordered by SEBI should not ordinarily go into an examination of the appropriateness of the assigned ratings on the merits. Inspections to judge the appropriateness of the ratings may be ordered by SEBI, only in case of complaints which are serious in nature to be carried out either by the officers of SEBI or independent experts with relevant experience or combination of both.

Notice of Inspection or Investigation

SEBI shall give ten days written notice to the credit rating agency before ordering an inspection or investigation. SEBI in the interest of the investors may order in writing, direct that the inspection or investigation of the affairs of the credit rating agency to be taken up without such notice.

Obligations of Credit Rating Agency

- Every CRAs shall be the duty of whose affairs are being inspected or investigated, and of every director, officer or employee thereof, to produce to the inspecting or investigating officer such books, accounts and other documents in its or his custody or control and furnish him with such statements and information relating to its rating activities, as the inspecting officer may require within such reasonable period as may be specified by the said officer.
- The credit rating agency shall –
 - (a) allow the inspecting officer to have reasonable access to the premises occupied by such credit rating agency or by any other person on its behalf;
 - (b) extend to the inspecting officer reasonable facility for examining any books, records, documents and computer data in the possession of the credit rating agency; and
 - (c) provide copies of documents or other materials which, in the opinion of the inspecting officer, are relevant for the purposes of the inspection or investigation, as the case may be.
- The inspecting officer, in the course of inspection or investigation, shall be entitled to examine, or record the statements, of any officer, director or employee of the credit rating agency for the purposes connected with the inspection or investigation.
- Every director, officer or employee of the credit rating agency shall be bound to render to the inspecting officer all assistance in connection with the inspection or investigation which the inspecting officer may reasonably require.

Submission of Report

The inspecting officer should as soon as possible, on completion of the inspection or investigation, submit a report to SEBI. However, if directed to do so by SEBI, he may submit an interim report.

Action on Inspection and Investigation

A credit rating agency which –

- (a) fails to comply with any condition subject to which a certificate has been granted;
- (b) contravenes any of the provisions of the Act or these regulations or any other regulations made under the Act; shall be dealt with in the manner provided under Chapter V of the Securities and Exchange Board of India (Intermediaries) Regulations, 2008.

SEBI or the chairman shall after consideration of inspection or investigation report take such action as SEBI or the chairman may deem fit and appropriate including action under chapter V of the SEBI (Intermediaries) Regulations, 2008.

TRANSPARENCY & DISCLOSURE NORMS FOR CREDIT RATING AGENCIES

Recent events in global financial system have underlined the pivotal role that credit ratings play. 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 in consultation with the CRAs, prescribed the following transparency and disclosure norms for the CRAs.

Rating Process

A CRA shall keep the following records in support of each credit rating and review / surveillance thereof:

- The important factors underlying the credit rating and sensitivity of such credit rating to changes in these factors;
- Summary of discussions with the issuer, its management, auditors and bankers which have a bearing on the credit rating;
- Decisions of the rating committee(s), including voting details and notes of dissent, if any, by any member of the rating committee, and
- If a quantitative model is 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.

Any change in the rating process or policies shall be disclosed in the CRA's website, to enable the investors to discern the changes made to the same.

These records should be maintained till five years after maturity of instruments and be made available to auditors and regulatory bodies when sought by them.

Default Studies

The CRA, should publish information about the historical default rates of CRA rating categories and whether the default rates of these categories have changed over time, so that the public can understand the historical performance of each category and if and how rating categories have changed, and be able to draw quality comparisons among ratings given by different CRAs. The default rates shall be calculated in the following manner:

- One Year Default Rate is the weighted average of default rates of all possible 1 year static pools in the 5-year period.
- Cumulative Default Rate: The cumulative default rate (CDR) represents the likelihood of an entity that was rated at the beginning of any multi-year period defaulting at any time during the multi-year period. Three-year cumulative default rate shall be computed as: $\text{Three-year CDR for rating category X} = \frac{\text{No. of issuers which defaulted over the three-year period}}{\text{No. of issuers outstanding at the beginning of the three-year period}}$.

Here,

Static Pool:	Non-defaulted ratings that were outstanding at the beginning of any period.
Default:	Non-payment of interest or principal amount in full on the pre-agreed date. A CRA shall recognize default at the first instance of delay in servicing of interest or principal on the rated debt instrument.
Default Rate:	The number of defaults among rated entities in the static pool as a percentage of the total number of entities in the static pool.
Averaging:	All averaging across static pools for default rate computations must be based on the weighted average method where the weights are the number of ratings in each static period.

Dealing with Conflict of Interest

A CRA shall formulate the policies and internal codes for dealing with the conflict of interests. A CRA shall ensure that 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, the employees' involved in the credit rating process and their dependants do not have ownership of the shares of the issuer and prompt review of the credit ratings of the securities as and when any of its employees joins the respective issuer.

Obligations in Respect of Rating of Structured Finance Products

A CRA may undertake rating of structured finance products, namely, instruments/ pay-outs resulting from securitization transactions. In such cases, apart from following all the applicable requirements in case of non-structured ratings, the following additional requirements shall also be complied with:

- A CRA or its subsidiaries shall not provide consultancy or advisory services regarding the design of the structured finance instrument.
- The rating symbols shall clearly indicate that the ratings are for structured finance products.

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. A CRA shall monitor and disclose credit rating during the life of the rated securities, as if it were a solicited rating.

Disclosures

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 kept on their websites. Where a specific format has been prescribed, the disclosures shall be made in that format. A CRA shall make all the disclosures stipulated below on their websites:

- A CRA shall formulate and disclose its policies, methodology and procedures in detail regarding solicited and unsolicited credit ratings;
- A CRA shall disclose in the formats prescribed about details of new credit ratings assigned during last six-months; Movement of credit rating of all outstanding securities during the last six-months;
- Movement of each credit rating;
- Movement of each credit rating from investment grade to non investment grade and vice versa
- Movement of each credit rating that has moved by more than one notch;
- The history of credit rating of all outstanding securities;
- On annual basis, the list of defaults separately for each rating category (e.g. AAA, AA, A, BBB, BB, B, C) This shall include the initial credit rating assigned by the CRA, month and year of initial rating, month and year of default, last credit rating assigned by the CRA before the issuer defaulted, comments of CRAs, if any.
- On annual basis, the average one-year and three-year cumulative default rates (based on weighted average), for the last 5 years, separately for each following category:
 - ▶ each credit rating category (e.g. AAA, AA, A, BBB, BB, B, C), separately;
 - ▶ structured instruments and non-structured instruments, separately
- A CRA shall disclose the general nature of its compensation arrangements with the issuers.

- A CRA shall disclose, in case of accepted ratings, its conflict of interest, if any, including the details of relationship – commercial or otherwise – between the issuer whose securities are being rated / any of its associate of such issuer and the CRA or its subsidiaries.
- A CRA shall disclose annually its total receipt from rating services and non-rating services, issuer wise percentage share of non-rating income of the CRA and its subsidiary to the total revenue of the CRA and its subsidiary from that issuer, and names of the rated issuers who along with their associate contribute 10% or more of total revenue of the CRA and its subsidiaries.
- While publishing the ratings of structured finance products and their movements, a CRA apart from following all the applicable requirements in case of non-structured ratings shall also disclose the track record of the originator and details of nature of underlying assets while assigning the credit rating. The track record shall include a brief description of the financials of the originator, rating migrations to speculative categories and defaults.
- A CRA shall also disclose at least once in every six months, the performance of the rated pool, i.e., collection efficiency, delinquencies. A CRA shall also provide a detailed description of the underlying pools including ageing, Credit enhancements such as liquidity supports, first and second loss guarantee provided shall also be disclosed.
- While publishing unsolicited ratings and their movements, a CRA apart from following all the applicable requirements in case of solicited ratings shall make the following disclosures:
 - ▶ the extent of participation by the issuer, its management, bankers and auditors in the credit rating process.
 - ▶ the information used and its source in arriving at and reviewing the credit rating.
- A CRA shall disclose annually all the unsolicited ratings carried out in the last three financial years; names of issuers, which were given, solicited rating in the last financial year.
- A CRA shall disclose its shareholding pattern as prescribed by stock exchanges for a listed company under clause 35 of Listing Agreement.
- A CRA shall disclose the compliance status of each provision of IOSCO code of conduct.

Implementation Schedule and Reporting

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

A CRA can make additional disclosures other than those stipulated with the prior approval of its Board.

Points to Remember

If a company make a public issue of convertible debentures it has to obtained credit rating from one or more credit rating agencies. But in case of issue of equity shares it is optional.

Apart from the above mentioned guidelines. SEBI had also prescribed guidelines for dealing with conflict of interest for investment trading by CRAs, Access persons and other employees.

INTERNAL AUDIT OF CREDIT RATING AGENCY

SEBI in consultation with the credit rating agencies (CRAs) prescribed that an internal audit on a half yearly basis to be undertaken by the CRAs which is envisaged under Regulation 22 of the SEBI (Credit Rating Regulations), 1999 by Company Secretaries, Chartered Accountants, or Cost and Management Accountants who are in practice and who do not have any conflict of interest with the CRA. It shall cover all aspects of CRA operations and procedures, including investor grievance redressal mechanism, compliance with the requirements

stipulated in the SEBI Act, Rules and Regulations made thereunder, and guidelines issued by SEBI from time to time. The report shall state the methodology adopted, deficiencies observed, and consideration of response of the management on the deficiencies and also include a summary of operations and of the audit, covering the size of operations, number of transactions audited and the number of instances where violations/deviations were observed while making observations on the compliance of any regulatory requirement. The report shall comment on the adequacy of systems adopted by the CRA for compliance with the requirements of regulations and guidelines issued by SEBI and investor grievance redressal.

The time schedule for the internal audit shall be as under:

- The CRA shall receive the report of the internal audit within two months from the end of the half-year.
- The Board of Directors of the CRA shall consider the report and take steps to rectify the deficiencies, if any, and the CRA shall send an Action Taken Report to SEBI within next two months.

RATING SYMBOLS AND DEFINITIONS

SEBI observed that the Credit Rating Agencies registered with it use different rating symbols and definitions. So there was a need to be common rating symbols and definitions (i) for easy understanding of the rating symbols and their meanings by the investors, and (ii) to achieve high standards of integrity and fairness in ratings. SEBI in consultation with the CRAs and on the recommendation of its Corporate Bonds and Securitisation Advisory Committee, standardised rating symbols and their definitions have been devised for the following :

- (a) Long term debt instruments
- (b) Short term debt instruments
- (c) Long term structured finance instruments
- (d) Short term structured finance instruments
- (e) Long term mutual fund schemes and
- (f) Short term mutual fund schemes.

Rating symbols should have CRA's first name as prefix. For Example : CARE AAA, CARE AA etc.

Long Term Debt Instruments

These instruments are with original maturity exceeding one year.

- | | |
|------------|--|
| AAA | – Instruments with this rating are considered to have the highest degree of safety regarding timely servicing of financial obligations. Such instruments carry lowest credit risk. |
| AA | – Instruments with this rating are considered to have high degree of safety regarding timely servicing of financial obligations. Such instruments carry very low credit risk. |
| A | – Instruments with this rating are considered to have adequate degree of safety regarding timely servicing of financial obligations. Such instruments carry low credit risk. |
| BBB | – Instruments with this rating are considered to have moderate degree of safety regarding timely servicing of financial obligations. Such instruments carry moderate credit risk. |
| BB | – Instruments with this rating are considered to have moderate risk of default regarding timely servicing of financial obligations. |
| B | – Instruments with this rating are considered to have high risk of default regarding timely servicing of financial obligations. |
| C | – Instruments with this rating are considered to have very high risk of default regarding timely servicing of financial obligations. |

- D** – Instruments with this rating are in default or are expected to be in default soon.

Modifiers {"+" (plus) / "-"(minus)} can be used with the rating symbols for the categories AA to C. The modifiers reflect the comparative standing within the category.

Short Term Debt Instruments

These instruments are with original maturity of upto one year. Rating symbols should have CRA's first name as prefix.

- A1** – Instruments with this rating are considered to have very strong degree of safety regarding timely payment of financial obligations. Such instruments carry lowest credit risk.
- A2** – Instruments with this rating are considered to have strong degree of safety regarding timely payment of financial obligations. Such instruments carry low credit risk.
- A3** – Instruments with this rating are considered to have moderate degree of safety regarding timely payment of financial obligations. Such instruments carry higher credit risk as compared to instruments rated in the two higher categories.
- A4** – Instruments with this rating are considered to have minimal degree of safety regarding timely payment of financial obligations. Such instruments carry very high credit risk and are susceptible to default.
- D** – Instruments with this rating are in default or expected to be in default on maturity.

Modifier {"+" (plus)} can be used with the rating symbols for the categories A1 to A4. The modifier reflects the comparative standing within the category.

Long Term Structured Finance Instruments

These instruments are with original maturity exceeding one year.

- AAA (SO)** – Instruments with this rating are considered to have the highest degree of safety regarding timely servicing of financial obligations. Such instruments carry lowest credit risk.
- AA (SO)** – Instruments with this rating are considered to have high degree of safety regarding timely servicing of financial obligations. Such instruments carry very low credit risk.
- A (SO)** – Instruments with this rating are considered to have adequate degree of safety regarding timely servicing of financial obligations. Such instruments carry low credit risk.
- BBB (SO)** – Instruments with this rating are considered to have moderate degree of safety regarding timely servicing of financial obligations. Such instruments carry moderate credit risk.
- BB(SO)** – Instruments with this rating are considered to have moderate risk of default regarding timely servicing of financial obligations.
- B(SO)** – Instruments with this rating are considered to have high risk of default regarding timely servicing of financial obligations.
- C (SO)** – Instruments with this rating are considered to have very high likelihood of default regarding timely payment of financial obligations.
- D (SO)** – Instruments with this rating are in default or are expected to be in default soon.

Modifiers {"+" (plus) / "-"(minus)} can be used with the rating symbols for the categories AA(SO) to C(SO). The modifiers reflect the comparative standing within the category.

Short Term Structured Finance Instruments

The instruments with original maturity of upto one year.

- A1 (SO) – Instruments with this rating are considered to have very strong degree of safety regarding timely payment of financial obligation. Such instruments carry lowest credit risk.
- A2 (SO) – Instruments with this rating are considered to have strong degree of safety regarding timely payment of financial obligation. Such instruments carry low credit risk.
- A3 (SO) – Instruments with this rating are considered to have moderate degree of safety regarding timely payment of financial obligation. Such instruments carry higher credit risk as compared to instruments rated in the two higher categories.
- A4 (SO) – Instruments with this rating are considered to have minimal degree of safety regarding timely payment of financial obligation. Such instruments carry very high credit risk and are susceptible to default.
- D (SO) – Instruments with this rating are in default or expected to be in default on maturity.

Modifier {"+" (plus)} can be used with the rating symbols for the categories A1(SO) to A4(SO). The modifier reflects the comparative standing within the category.

Long Term Debt Mutual Fund Schemes

These debt mutual fund schemes have an original maturity exceeding one year. Rating symbols should have CRA's first name as prefix.

- AAAmfs – Schemes with this rating are considered to have the highest degree of safety regarding timely receipt of payments from the investments that they have made.
- AAmfs – Schemes with this rating are considered to have the high degree of safety regarding timely receipt of payments from the investments that they have made.
- Amfs – Schemes with this rating are considered to have the adequate degree of safety regarding timely receipt of payments from the investments that they have made.
- BBBmfs – Schemes with this rating are considered to have the moderate degree of safety regarding timely receipt of payments from the investments that they have made.
- BBmfs – Schemes with this rating are considered to have moderate risk of default regarding timely receipt of payments from the investments that they have made.
- Bmfs – Schemes with this rating are considered to have high risk of default regarding timely receipt of payments from the investments that they have made.
- Cmfs – Schemes with this rating are considered to have very high risk of default regarding timely receipt of payments from the investments that they have made.

Modifiers {"+" (plus) / "-" (minus)} can be used with the rating symbols for the categories AAmfs to Cmfs. The modifiers reflect the comparative standing within the category.

Short Term Debt Mutual Fund Schemes

These debt mutual fund schemes that have an original maturity of upto one year. Rating symbols should have CRA's first name as prefix.

- A1mfs – Schemes with this rating are considered to have very strong degree of safety regarding timely receipt of payments from the investments that they have made.

- A2mfs – Schemes with this rating are considered to have strong degree of safety regarding timely receipt of payments from the investments that they have made.
- A3mfs – Schemes with this rating are considered to have moderate degree of safety regarding timely receipt of payments from the investments that they have made.
- A4mfs – Schemes with this rating are considered to have minimal degree of safety regarding timely receipt of payments from the investments that they have made.

Modifier {"+" (plus)} can be used with the rating symbols for the categories A1mfs to A4mfs. The modifier reflects the comparative standing within the category.

IPO GRADING

IPO grading (Initial Public Offering Grading) is a service aimed at facilitating the assessment of equity issues offered to public. The grade assigned to any individual issue represents a relative assessment of the 'fundamentals' of that issue in relation to the universe of other listed equity securities in India. Such grading is assigned on a five-point scale with a higher score indicating stronger fundamentals.

IPO Grade 1 – Poor Fundamentals

IPO Grade 2 – Below - Average Fundamentals

IPO Grade 3 – Average Fundamentals

IPO Grade 4 – Above-average fundamentals

IPO Grade 5 – Strong fundamentals

IPO grading is different from an investment recommendation. Investment recommendations are expressed as 'buy', 'hold' or 'sell' and are based on a security specific comparison of its assessed 'fundamentals factors' (business prospects, financial position etc.) and 'market factors' (liquidity, demand supply etc.) to its price. On the other hand, IPO grading is expressed on a five-point scale and is a relative comparison of the assessed fundamentals of the graded issue to other listed equity securities in India.

As the IPO grading does not take cognizance of the price of the security, it is not an investment recommendation. Rather, it is one of the inputs to the investor to aiding in the decision making process.

As per SEBI (ICDR) Regulations, every unlisted company obtaining grading for IPO shall disclose all the grades obtained, along with the rationale discretion furnished by the credit rating agency(ies) for each of the grades obtained, in the prospectus, abridged prospectus, issue advertisements and at all other places where the issuer company is advertising for the IPO.

SEBI has been taking a pioneering role in investor protection by increasing disclosure levels by entities seeking to access equity markets for funding. This has caused India to be amongst one of the more transparent and efficient capital markets in the world. However, these disclosures demand fairly high levels of analytical sophistication of the reader in order to effectively achieve the goal of information dissemination.

IPO grading is positioned as a service that provides 'an independent assessment of fundamentals' to aid comparative assessment that would prove useful as an information and investment tool for investors. Moreover, such a service would be particularly useful for assessing the offerings of companies accessing the equity markets for the first time where there is no track record of their market performance.

As mentioned above, the IPO grade assigned to any issue represents a relative assessment of the 'fundamentals' of that issue in relation to the universe of other listed equity securities in India. This grading can be used by the investor as tool to make investment decision. The IPO grading will help the investor better appreciate the meaning of the disclosures in the issue documents to the extent that they affect the issue's fundamentals. Thus, IPO grading is an additional investor information and investment guidance tool.

Procedure for IPO Grading

Credit Rating agencies (CRAs) registered with SEBI will carry out IPO grading.

SEBI does not play any role in the assessment made by the grading agency. The grading is intended to be an independent and unbiased opinion of that agency.

It is intended that IPO fundamentals would be graded on a five point scale from grade 5 (indicating strong fundamentals) to grade 1 (indicating poor fundamentals). The grade would read as: "Rating Agency name" IPO Grade 1 viz. CARE IPO Grade 1, CRISIL IPO Grade 1 etc.

The assigned grade would be a one time assessment done at the time of the IPO and meant to aid investors who are interested in investing in the IPO. The grade will not have any ongoing validity.

The company needs to first contact one of the grading agencies and mandate it for the grading exercise. The agency would then follow the process outlined below.

- Seek information required for the grading from the company.
- On receipt of required information, have discussions with the company's management and visit the company's operating locations, if required.
- Prepare an analytical assessment report.
- Present the analysis to a committee comprising senior executives of the concerned grading agency. This committee would discuss all relevant issues and assign a grade.
- Communicate the grade to the company along with an assessment report outlining the rationale for the grade assigned.

Though this process will ideally require 2-3 weeks for completion, it may be a good idea for companies to initiate the grading process about 6-8 weeks before the targeted IPO date to provide sufficient time for any contingencies.

Points to Remember

IPO grading is optional as per SEBI (ICDR) Regulations, 2009 w.e.f. February 04, 2014

LESSON ROUND UP

- Credit rating is the evaluation of the credit worthiness of an individual or of a business concern or of an instrument of a business based on relevant factors indicating ability and willingness to pay obligations as well as net worth.
- The main purpose of credit rating is to communicate to the investors the relative ranking of the default loss probability for a given fixed income investment, in comparison with other rated instruments.
- In India CRISIL (Credit Rating and Information Services (India) Limited) was set up as the first credit rating agency in 1987. This was followed by ICRA Limited (Investment Information and Credit Rating Agency of India Limited) in 1991 and CARE (Credit Analysis and Research Limited) in 1994, in 1999 Fitch Rating India Pvt. Ltd. now known as India Ratings and Research Pvt. Ltd, Brickwork Ratings Pvt. Ltd. in 2008, SMERA (SME Rating Agency of India Limited) and Infomerics Valuation and Ratings Pvt. Ltd. in 2011. All these six credit rating agencies are registered with the Securities and Exchange Board of India.
- Credit Rating Agencies are regulated by SEBI (Credit Rating Agencies) Regulations, 1999.
- SEBI has also prescribed Transparency and Disclosure Norms (Guidelines) for Credit Rating Agencies.
- Practising Company Secretaries are authorized to undertake Internal Audit of CRAs.

- SEBI in consultation with the CRAs and considering the international practices, standardised the Credit Rating Symbols and their definitions for different instruments.
- IPO grading (Initial Public Offering Grading) is a service aimed at facilitating the assessment of equity issues offered to public.
- IPO grading is optional for public issue w.e.f. February 04, 2014.

GLOSSARY

Acid Test Ratio	The value of cash equivalents and accounts receivable (the quick assets) divided by current liabilities. Also known as quick asset ratio or liquidity ratio, it is a measurement of corporate liquidity.
Credit Rating Agency	Credit rating agency means a body corporate which is engaged in, or proposes to be engaged in, the business of rating of securities offered by way of public or rights issue.
Credit Risk	The risk that a counter party will not settle an obligation for full value, either when due or at anytime thereafter. Credit risk includes pre-settlement risk (replacement cost risk) and settlement risk (principle risk)
Securitization	The process of homogenizing and packaging financial instruments into a new fungible one. Acquisition, classification, collateralization, composition, pooling and distribution are functions within this process.
Net Worth	The aggregate value of paid up capital and free reserves (excluding reserves created out of revaluation), reduced expenditure, not written off including miscellaneous expenses not written off.

SELF TEST QUESTIONS

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation.)

1. What do you understand by credit rating.
2. Explain major provisions of SEBI (Credit Rating Agencies) Regulations, 1999.
3. Explain general obligations of Credit Rating Agencies under Chapter III of SEBI (Credit Rating Agencies) Regulations, 1999.
4. Discuss the procedure relating to inspection and investigation of the credit rating agencies.
5. Explain important uses of credit rating and factors contributing to the success of a rating system.
6. Briefly discuss the disclosures required to be made by a Credit Rating Agency (CRA) under the Guidelines issued by SEBI for CRAs.
7. What is IPO Grading? Discuss briefly the procedure for grading of IPO.

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Lesson 4

Market Infrastructure Institutions – Stock Exchange Trading Mechanism

LESSON OUTLINE

- Introduction
- Stock Exchange Trading Mechanism
- Short Selling and Securities Lending and Borrowing
- Bombay Stock Exchange Ltd.
- Basket Trading System
- National Stock Exchange of India Ltd. (NSEIL)
- Straight Through Processing
- Direct Market Access
- Demutualization of Stock Exchange
- SME Exchange
- Institutional Trading Platform (ITP)
- Dedicated Debt Segment on Stock Exchange
- Algorithmic Trading
- LESSON ROUND UP
- GLOSSARY
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

Stock exchange is taken as a barometer of the economy of a country. It is the most dynamic and organised component of capital market. Especially, in developing countries like India, the stock exchanges play a cardinal role in promoting the level of capital formation through effective mobilisation of savings and ensuring investment safety. It is equally important to have the understanding of the governance of Stock Exchanges, and the services they provide to investors.

This lesson will enable the students to understand the Operation of stock exchanges, Stock Exchange Trading Mechanism, Short Selling and Securities Lending and Borrowing, Straight Through Processing, Direct Market Access and Algorithmic Trading, Demutualization of Stock Exchange, SME Exchange and advantages of SME Exchange etc.

INTRODUCTION

There are 19 stock exchanges at present in India. All of them are regulated in terms of Securities Contract (Regulation) Act, 1956 and SEBI Act, 1992 and the rules and regulations made thereunder. Some of the exchanges started as voluntary non-profit associations such as Bombay Stock Exchange (BSE) and Indore Stock Exchange. The Stock Exchanges at Chennai, Jaipur, Hyderabad and Pune were incorporated as companies limited by guarantee. The other stock exchanges are companies limited by shares and incorporated under the Companies Act, 1956 (now Companies Act, 2013) or earlier acts.

Pursuant to Section 131 of the Finance Act, 2015 and Central Government Notification F. No. 1/9/SM/2015 dated 28th August, 2015 all recognized association (commodity derivatives exchanges) under the Forwards Contracts Act, 1952 and deemed to recognized stock exchange under the SCRA, 1956.

The stock exchanges are managed by Board of Directors or Council of Management consisting of elected brokers and representatives of Government and Public appointed by SEBI. The Boards of stock exchanges are empowered to make and enforce rules, bye-laws and regulations with jurisdiction over all its members.

The Acts, Rules and Regulations governing the stock exchanges have been separately discussed in a lesson in of this study material.

Membership of stock exchanges is generally given to persons financially sound and with adequate experience/ training in stock market. Their enrolment as member is regulated and controlled by SEBI to whom they have to pay an annual charge. A member of the stock exchange is called 'broker' who can transact on behalf of his clients as well as on his own behalf. A non-member can deal in securities only through members. A broker can also take the assistance of sub-broker whom he can appoint under the procedure of registration.

STOCK EXCHANGE TRADING MECHANISM

The stock exchange is a key institution facilitating the issue and sale of various types of securities. It is a pivot around which every activity of the capital market revolves. In the absence of the stock exchange, the people with savings would hardly invest in corporate securities for which there would be no liquidity (buying and selling facility). Corporate investments from the general public would have been thus lower.

Stock exchanges thus represent the market place for buying and selling of securities and ensuring liquidity to them in the interest of the investors. The stock exchanges are virtually the nerve centre of the capital market and reflect the health of the country's economy as a whole.

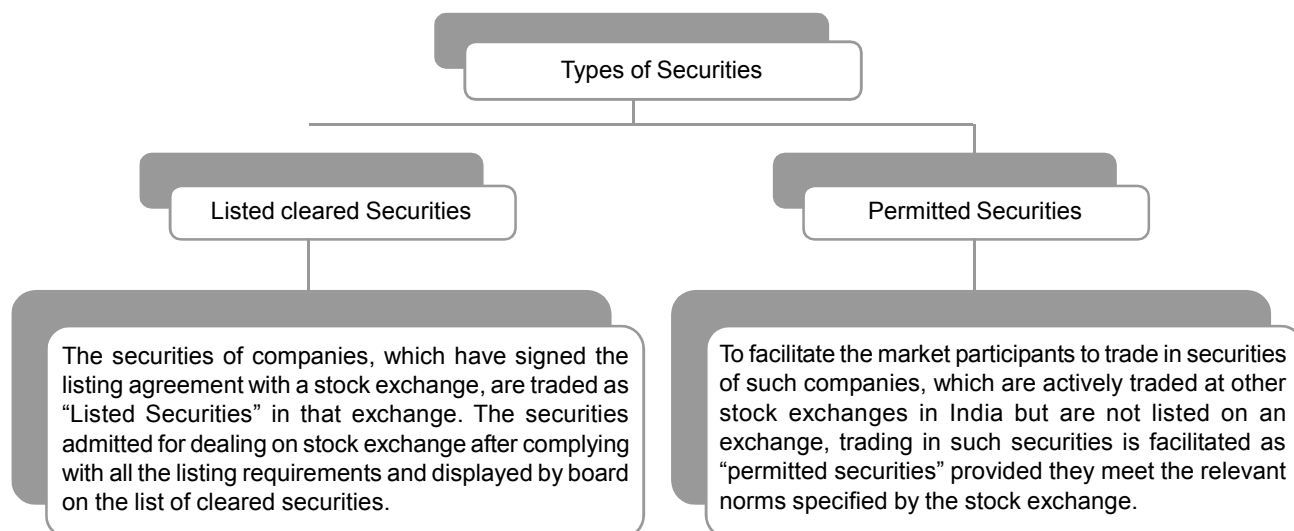
Securities are traded in three different ways in stock exchanges ring, namely—settlement basis, spot basis and cash basis.

Shares of companies which are not in the spot list are known as 'cash' shares or 'B' Category shares. They are traded on cash basis or delivery basis and cannot be traded on settlement basis. The actual delivery of securities and payment has to be made on or before the settlement date fixed in the case of cash basis trading.

As far as spot trading is concerned the actual delivery of securities must be made to the buying broker within 48 hours of the contract. It is expected that the seller would be paid by the buyer immediately on delivery of securities.

All securities whether the specified list or cash list can be traded on spot basis or cash basis.

Types of Securities



Types of Delivery

Types of delivery in the stock exchanges are spot delivery, hand delivery and special delivery.

Spot Delivery	Where the delivery of and payment for securities are to be made on the same day as the day of contract or on the next day.
Hand Delivery	Where the delivery of and payment are to be made on the delivery date fixed by the stock exchange authorities.
Special Delivery	Where delivery and payment made after the delivery date fixed by the stock exchange authorities.

Just as we are faced with day to day uncertainties pertaining to weather, health, traffic etc and take steps to minimize the uncertainties, so also in the stock markets, there is uncertainty in the movement of share prices. This uncertainty leading to risk is sought to be addressed by margining systems by stock markets.

Suppose an investor, purchases 1000 shares of ‘xyz’ company at Rs.100/- on January 1, 2017. Investor has to give the purchase amount of Rs.1,00,000/- (1000 x 100) to his broker on or before January 2, 2017. Broker, in turn, has to give this money to stock exchange on January 3, 2017.

There is always a small chance that the investor may not be able to bring the required money by required date. As an advance for buying the shares, investor is required to pay a portion of the total amount of Rs.1,00,000/- to the broker at the time of placing the buy order. Stock exchange in turn collects similar amount from the broker upon execution of the order. This initial token payment is called margin.

Remember, for every buyer there is a seller and if the buyer does not bring the money, seller may not get his / her money. Margin is levied on the seller also to ensure that he / she gives the 100 shares sold to the broker who in turn gives it to the stock exchange.

Margin payments ensure that each investor is serious about buying or selling shares.

In the above example, assume that margin was 15%. That is investor has to give Rs.15,000/- (15% of Rs.1,00,000) to the broker before buying. Now suppose that investor bought the shares at 11 am on January 1, 2017. Assume that by the end of the day price of the share falls by Rs.25/-. That is total value of the shares has come down to

Rs.75,000/-. That is buyer has suffered a notional loss of Rs.25,000/-. In our example buyer has paid Rs.15,000/- as margin but the notional loss, because of fall in price, is Rs.25,000/-. That is notional loss is more than the margin given.

In such a situation, the buyer may not want to pay Rs.1,00,000/- for the shares whose value has come down to Rs.75,000/-.

Similarly, if the price has gone up by Rs.25/-, the seller may not want to give the shares at Rs.1,00,000/-. To ensure that both buyers and sellers fulfil their obligations irrespective of prices movements, notional losses are also need to be collected. Prices of shares may keep on moving every day. Margins ensure that buyers bring money and sellers bring shares to complete their obligations even though the prices have moved down or up.

Margins

An advance payment of a portion of the value of a stock transaction. The amount of credit a broker or lender extends to a customer for stock purchase.

Margin Trading

Margin trading was introduced by SEBI to curb speculative dealings in shares leading to volatility in the prices of securities.

“Initial margin” in this context means the minimum amount, calculated as a percentage of the transaction value, to be placed by the client, with the broker, before the actual purchase. The broker may advance the balance amount to meet full settlement obligations.

“Maintenance margin” means the minimum amount, calculated as a percentage of market value of the securities, calculated with respect to last trading day's closing price, to be maintained by client with the broker.

When the balance deposit in the client's margin account falls below the required maintenance margin, the broker shall promptly make margin calls. However, no further exposure can be granted to the client on the basis of any increase in the market value of the securities.

The broker may liquidate the securities if the client fails to meet the margin calls made by the broker or fails to deposit the cheques on the day following the day on which the margin call has been made or the cheque has been dishonoured.

The broker may also liquidate the securities in case the client's deposit in the margin account (after adjustment for mark to market losses) falls to 30% or less of the latest market value of the securities, in the interregnum between making of the margin call and receipt of payment from the client.

The broker must disclose to the stock exchange details on gross exposure including the name of the client, unique identification number, name of the scrip and if the broker has borrowed funds for the purpose of providing margin trading facilities, name of the lender and amount borrowed, on or before 12 Noon on the following day.

Stock exchanges disclose scripwise gross outstanding in margin accounts with all brokers to the market. Such disclosures regarding margin trading done on any day shall be made available after the trading hours on the following day through the website.

Characterstics of Margin

- Margin trading acts as a check on the tendency of clients to manipulate markets by placing orders on brokers without having adequate money or securities to backup the transaction.
- Margin trading will also acts as a curb on short selling and short buying.
- Margin trading mechanism also ensures transparency in dealings in securities and public exposure of the information regarding the backing behind all major securities transactions.
- In the Indian capital markets particularly excessive short selling and market positioning have been rampant. Margin trading has acted as a stabilising force.

Book Closure and Record Date

Book closure is the periodic closure of the Register of Members and Transfer Books of the company, to take a record of the shareholders to determine their entitlement to dividends or to bonus or right shares or any other rights pertaining to shares. Record date is the date on which the records of a company are closed for the purpose of determining the stock holders to whom dividends, proxies rights etc. are to be sent.

In accordance with Section 91 of the Companies Act, 2013 a company may close the register of members for a maximum of 45 days in a year and for not more than 30 days at any one time. Book closure is necessary for the purpose of paying dividend, making rights issue or bonus issue. The listed company is required to give notice of book closure in a news paper at least 7 days before the commencement of the book closure. The members whose names appear in the register of members on the last date of book closure are entitled to receive the benefits of dividend, right shares or bonus shares as the case may be.

Trading of Partly Paid Shares and Debentures

Companies fix the last date for payment of allotment or call money in case of partly paid shares or debentures and intimate this to all the stock exchanges wherein such shares or debentures are listed. Based on the date fixed by the company, the stock exchanges determine the settlement date upto which transactions in the scrip will be deemed to be good for delivery. After the said date, transactions in the securities take place only if they are paid up to the extent money has been called up.

Trend Line

When the price of shares moves in a particular direction which persists for a period of time, a price line is regarded as established. When the movement is upward, the trend is called 'BULLISH' and when the movement is downward it is called 'BEARISH'. Bear market is a weak or falling market characterised by the dominance of sellers. Whereas Bull market is a rising market with abundance of buyers and relatively few sellers.

Secondary movements that reverse the uptrend temporarily are known as reactions. The movements that reverse the down trend temporarily are known as rallies. When an uptrend breaks in the downward direction, it is called trend reversal.

Trading Volume

Trading volumes confirm whether the rise or fall in prices is in line with the trend. The high trading volume is built on rising prices, similarly the high trading volume is also linked with fall in prices. They respectively reflect a BULLISH trend and a BEARISH trend.

Turnover and Outstanding Position

The net turnover and outstanding positions in various scrips show the extent of BULLISH interest in them and are used along with trading volume to judge the intensity of the phase whether BULLISH or BEARISH. In a BULL phase there will be a sharp rise in the daily turnover of key scrips and in a BEAR phase the reverse will be the case.

MARKET MAKING

Market making is a process where the market makers offers a two way quote (both buy and sell) to increase the supply and demand of the scrip. This increase the liquidity in the stock.

Market-making is aimed at infusing liquidity in securities that are not frequently traded on stock exchanges. A market-maker is responsible for enhancing the demand supply situation in securities such as stocks and futures & options (F&O). To understand this concept better, it would be helpful to have an idea about the existing screen based electronic trading system. In this system , orders placed by buyers and sellers are matched by a computer

system (run by stock exchanges). This system is beneficial for actively-traded stocks, but not for lesser-traded ones. Investors usually ignore thinly-traded stocks despite good fundamentals due to fears that they might not be able to trade more frequently in them. The introduction of the market-making facility could be a possible means to infuse liquidity into such shares. In overseas markets, a market-maker is usually a broker or an institution. As a result, there is an incentive for the broker to recommend securities for which he creates a market.

A market-maker usually is responsible for enhancing activity in a few chosen securities. In the process, the market-maker provides both a buy and a sell quote for his chosen securities. He profits from the spread between buy and sell quotes. For example, if the market-maker gives a bid-ask quote of ₹ 505-500 (which means the market-maker will buy from the market at ₹ 500 and sell at ₹ 505), then the profit is ₹ 5. For illiquid securities, the profit spreads are usually higher (within a regulator-prescribed band) because of the higher risk taken by the market-maker.

Market-makers are obligated to buy or sell the security at a price and size they have quoted. One may wonder the role of a market-maker in the computerised system, as investors can transact directly without a third party. The market-maker's role here is to ensure supply of stocks at any given point in time. Market-makers are helpful as they are always ready to buy or sell as long as investors are willing to pay the price quoted by them.

SECURITIES LENDING

This method is regulated by SEBI which introduced guidelines in 1997 for this purpose. Under the scheme, a person with idle shares can lend them to another who does not have the shares to fulfill his obligation under a trade finalised by him. There will be no direct contacts between the borrower and lender of securities. An intermediary who can guarantee the scheme and make good the loss in the borrower who fails to honour his obligations can alone provide substance to the scheme. The borrower has to put up collateral for his borrowings and pay cash margin levied on the securities by the authorities. Income from securities lending is exempt from Capital Gains Tax.

SECURITIES' LENDING AND BORROWING ('SLB')

Securities' Lending and Borrowing ('SLB') describes the market practice whereby securities are temporarily transferred by one party (the lender) to another (the borrower) via an approved intermediary.

The Borrower is obliged to return them either on demand or at the end of an agreed term and also has an option to early return. Lender may recall securities at any time within normal market settlement cycle. SLB is a major and growing activity which provides significant benefits for issuers, investors and traders alike. SLB helps in improving market liquidity, more efficient settlement, tighter dealer prices and perhaps a reduction in the cost of capital.

Why participate in Securities Lending & Borrowing ?

- Lender's Motivation
- It provides lender incremental return on an idle portfolio.
- Borrower's Motivation
- To cover a short position: avoidance of settlement failure.
- Hedging of futures & options positions.
- Borrow and lend to reap benefits of the market sentiment.

SHORT SELLING AND SECURITIES LENDING AND BORROWING

SEBI vide Circular no MRD/DoP/SE/Dep/Cir- 14 /2007 dated December 20, 2007 permitted all classes of investors to short sell subject to the broad framework specified there in which are enumerated as follows.

Broad Framework for Short Selling

- “Short selling” shall be defined as selling a stock which the seller does not own at the time of trade.
- All classes of investors, viz., retail and institutional investors, shall be permitted to short sell.
- Naked short selling shall not be permitted in the Indian securities market and accordingly, all investors would be required to mandatorily honour their obligation of delivering the securities at the time of settlement.
- No institutional investor shall be allowed to do day trading i.e., square-off their transactions intra-day. In other words, all transactions would be grossed for institutional investors at the custodians’ level and the institutions would be required to fulfill their obligations on a gross basis.
- The custodians, however, would continue to settle their deliveries on a net basis with the stock exchanges.
- The stock exchanges shall frame necessary uniform deterrent provisions and take appropriate action against the brokers for failure to deliver securities at the time of settlement which shall act as a sufficient deterrent against failure to deliver.
- A scheme for Securities Lending and Borrowing (SLB) shall be put in place to provide the necessary impetus to short sell. The introduction of fullfledged securities lending and borrowing scheme shall be simultaneous with the introduction of short selling by institutional investors.
- The securities traded in Future and Option (F&O) segment shall be eligible for short selling.
- SEBI may review the list of stocks that are eligible for short selling transactions from time to time.
- The institutional investors shall disclose upfront at the time of placement of order whether the transaction is a short sale. However, retail investors would be permitted to make a similar disclosure by the end of the trading hours on the transaction day.
- The brokers shall be mandated to collect the details on scrip-wise short sell positions, collate the data and upload it to the stock exchanges before the commencement of trading on the following trading day. The stock exchanges shall then consolidate such information and disseminate the same on their websites for the information of the public on a weekly basis.
- The frequency of such disclosure may be reviewed from time to time with the approval of SEBI.

Broad Framework for Securities Lending and Borrowing

- In order to provide a mechanism for borrowing of securities to enable settlement of securities sold short, the stock exchanges shall put in place, a full fledged securities lending and borrowing (SLB) scheme, within the overall framework of “Securities Lending Scheme, 1997” (the scheme), that is open for all market participants in the Indian securities market.
- To begin with, the SLB shall be operated through Clearing Corporation/ Clearing House of stock exchanges having nation-wide terminals who will be registered as Approved Intermediaries (AIs) under the SLS, 1997.
- Eligible scrips for SLB: In addition to the scrips on which derivatives contracts are available, scrips that fulfill the following criteria shall be considered eligible for SLB:
 - (a) Scrip classified as ‘Group I security’ as per SEBI circular MRD/DoP/SE/Cir-07/2005 dated February 23, 2005;

AND

- (b) Market Wide Position Limit (MWPL) of the scrip, as defined at para 12 (a) of Annexure 2 of the MRD/DoP/SE/Dep/Cir-14/2007 dated December 20, 2007, shall not be less than Rs.100 crores;

AND

- (c) Average monthly trading turnover in the scrip in the Cash Market shall not be less than Rs.100 crores in the previous six months.

- Event a scrip fails to meet the eligibility criteria, no new SLB transaction shall be allowed in the scrip from the next trading day. However, the existing contracts in such scrips shall be allowed to continue till expiry.
- The collateral to be accepted for meeting margin obligations related to SLB transactions shall be in the same form as applicable in the Cash Market.
- The SLB shall take place on an automated, screen based, order-matching platform which will be provided by the AIs. This platform shall be independent of the other trading platforms.
- To begin with, the securities traded in F&O segment shall be eligible for lending & borrowing under the scheme.
- Any lender or borrower who wishes to extend an existing lent or borrow position shall be permitted to roll-over such positions i.e. a lender who is due to receive securities in the pay out of an SLB session, may extend the period of lending. Similarly, a borrower who has to return borrowed securities in the pay-in of an SLB session, may, through the same SLB session, extend the period of borrowing. The roll-over shall be conducted as part of the SLB session.
- Rollover shall not permit netting of counter positions, i.e. netting between the 'borrowed' and 'lent' positions of a client.
- Roll-over shall be available for a period of 3 months i.e. the original contract plus 2 rollover contracts.
- Liquid Index Exchange Traded Funds (ETFs) shall be eligible for trading in the SLB segment.
- An Index ETF shall be deemed 'liquid' provided the Index ETF has traded on at least 80% of the days over the past 6 months and its impact cost over the past 6 months is less than or equal to 1%.
- All categories of investors including retail, institutional etc. will be permitted to borrow and lend securities. The borrowers and lenders shall access the platform for lending/borrowing set up by the AIs through the clearing members (CMs) (including banks and custodians) who are authorized by the AIs in this regard.
- The Authorised Intermediary (AIs) shall enter into an agreement with Clearing Members (CMs) for the purpose of facilitating lending and borrowing of securities.
- The agreement shall specify the rights, responsibilities and obligations of the parties to the agreement. The agreement shall include the basic conditions for lending and borrowing of securities as prescribed under SLB framework. Further, the exact role of AIs/CMs vis-à-vis the clients shall be laid down in the agreement. AIs shall ensure that there shall not be any direct agreement between the lender and the borrower.
- In addition to that, AIs may also include suitable conditions in the agreement to have proper execution, risk management and settlement of lending and borrowing transactions with clearing member and client.
- The AIs shall frame a rights and obligations document laying down the rights and obligation of CMs and clients for the purpose of lending and borrowing of securities. The rights and obligation document shall be mandatory and binding on the CMs and the clients for executing trade in the SLB framework.
- The AIs shall allot a unique ID to each client which shall be mapped to the Permanent Account Number

(PAN) of the respective clients. The AIs shall put in place appropriate systemic safeguards to ensure that a client is not able to obtain multiple client IDs.

- The tenure of lending/borrowing shall be fixed as standardised contracts. To start with, contracts with tenure of 30 trading days may be introduced.
- The settlement cycle for SLB transactions shall be on T+1 basis.
- The settlement of lending and borrowing transactions shall be independent of normal market settlement.
- The settlement of the lending and borrowing transactions shall be done on a gross basis at the level of the clients i.e. no netting of transactions at any level will be permitted.
- AIs would frame suitable risk management systems to guarantee delivery of securities to borrower and return of securities to the lender. In the case of lender failing to deliver securities to the AI or borrower failing to return securities to the AI, the AI shall conduct an auction for obtaining securities. In the event of exceptional circumstances resulting in non-availability of securities in auction, such transactions would be financially closed-out at appropriate rates, which may be more than the rates applicable for the normal close-out of transactions, so as to act as a sufficient deterrent against failure to deliver securities.
- Position limits at the level of market, CM and client shall be decided from time to time by AIs in consultation with SEBI. To begin with (a) the market-wide position limits for SLB transactions shall be 10% of the free-float capital of the company in terms of number of shares (b) No clearing member shall have open position of more than 10% of the market-wide position limits or ₹ 50 crore (base value), whichever is lower (c) For a FII/MF, the position limits shall be the same as of a clearing member (d) The client level position limits shall be not more than 1% of the market-wide position limits.
- There shall be no lending/borrowing activity during the periods of corporate action in the security and shall be disclosed by AI to the market.
- Any borrowing/lending and return of securities would not amount to purchase/disposal/transfer of the same for the purpose of compliance with the extant FDI/FII limits and the norms regarding acquisition of shares/ disclosure requirements specified under the various Regulations of SEBI.
- Adequate systems shall be put in place by the stock exchanges/Depositories to distinguish the SLB transactions from the normal market transactions in the demat system.
- AIs shall provide suitable arbitration mechanism for settling the disputes arising out of the SLB transactions executed on the platform provided by them.
- AIs shall disseminate in public domain, the details of SLB transactions executed on the platform provided by them and the outstanding positions on a weekly basis. The frequency of such disclosure may be reviewed from time to time with the approval of SEBI.

Settlement System

Settlement is the process of netting of transactions and actual delivery/receipt of securities and transfer deeds against receipts/payment of agreed amount. It is necessary to make a settlement to know the net effect of a series of transactions during a given period.

Settlement date is the date specified for delivery of securities between securities firms. For administrative convenience, a stock exchange divides the year into a number of settlement periods so as to enable members to settle their trades. All transactions executed during the settlement period are settled at the end of the settlement period.

Settlement risk or principal risk is the risk that the seller of a security or funds delivers its obligation but does not receive payment or that the buyer of a security or funds makes payment but does not receive delivery. In this event, the full principal value of the securities or funds transferred is at risk.

FAQ's on Settlement Cycle

UNDERSTANDING TRADE SETTLEMENT CYCLE

India is one of the most advanced markets when it comes to settlement of trade. The domestic market follows a T+2 settlement cycle. India is one of the most advanced markets when it comes to settlement of trade.

WHAT IS ROLLING SETTLEMENT?

In a rolling settlement, each trading day is considered as a trading period and trades executed during the day are settled based on net obligations for the day. In India, trades in rolling settlement are settled on a T+2 basis i.e. on the 2nd working day after a trade.

WHICH DAYS ARE CALCULATED FOR THE PURPOSE OF ROLLING SETTLEMENT?

For arriving at the settlement day, all intervening holidays, which include bank holidays, exchange holidays, Saturdays and Sundays, are excluded. Typically, trades taking place on Monday are settled on Wednesday, Tuesday's trades are settled on Thursday and so on.

WHEN DOES THE OPEN POSITIONS RESULT IN PAYMENT/ DELIVERY UNDER ROLLING SETTLEMENT?

Under rolling settlement, all open positions at the end of the day mandatorily result in payment/ delivery 'n' days later. Currently, trades in rolling settlement are settled on T+2 basis where T is the trade day. For example, a trade executed on Monday is mandatorily settled by Wednesday (considering two working days from the trade day).

Settlement Cycle for Rolling Settlement

	Activity	Day
Trading	Rolling settlement	T
Clearing	Custodial confirmation and delivery generation	T+1 working days
Settlement	Securities and funds pay-in and pay-out	T+2 working days
Post settlement	Auction	T+3 working days
	Bad delivery reporting	T+4 working days
	Auction settlement	T+5 working days
	Rectified bad delivery pay-in and pay-out	T+6 working days
	Re-bad delivery reporting and pick up	T+8 working days
	Close out of re-bad delivery and funds pay-in and pay-out	T+9 working days

For intraday traders, rolling settlement changes nothing. For institutional investors, who are forbidden to square off anyway, there would be no change. It is for retail investors who take leveraged positions across one night or more that rolling settlement has an impact. The funds and securities pay-in and pay-out are carried out on T+2 days

WHAT IS PAY-IN AND PAY-OUT?

Pay-in day is the day when the securities sold are delivered to the exchange by the sellers and funds for the securities purchased are made available to the exchange by the buyers. Pay-out day is the day the securities purchased are delivered to the buyers and the funds for the securities sold are given to the sellers by the exchange. At present, the pay-in and pay-out happens on the 2nd working day after the trade is executed on the exchange, that is settlement cycle is on T+2 rolling settlement.

WHAT IS NO-DELIVERY PERIOD?

Whenever a company announces a book closure or record date, the exchange set up a no-delivery period for that security. During this period only trading is permitted in the security. However, these trades are settled only after the no-delivery period is over. This is done to ensure that investor's entitlement for the corporate benefit is clearly determined.

WHAT IS AN AUCTION?

On account of non-delivery of securities by the trading member on the pay-in day, securities are put up for auction by the exchange. This ensures that buying trading member receives the securities. The Exchange purchases the requisite quantity in auction market and gives them to the buying trading member.

BOMBAY STOCK EXCHANGE LTD.

Bombay Stock Exchange Ltd., popularly known as "BSE" was established in 1875 as "The Native Share and Stock Brokers Association". It is the oldest one in Asia, even older than the Tokyo Stock Exchange, which was established in 1878. It is a voluntary non-profit making Association of Persons (AOP) and is currently engaged in the process of converting itself into demutualised and corporate entity. It has evolved over the years into its present status as the premier Stock Exchange in the country. It is the first Stock Exchange in the Country to have obtained permanent recognition in 1956 from the Govt. of India under the Securities Contracts (Regulation) Act, 1956.

The Exchange, provides market for trading in securities, debt and derivatives upholds the interests of the investors and ensures redressal of their grievances whether against the companies or its own member-brokers. It also strives to educate and enlighten the investors by conducting investor education programmes and making available to them necessary informative inputs.

Trading at BSE

The scrips traded on BSE have been classified into various groups.

BSE has, for the guidance and benefit of the investors, classified the scrips in the Equity Segment into A, B, E, P, T, XC, XD, XT, Z, F, G and M/MT groups on certain qualitative and quantitative parameters.

"A" Group	It is the most tracked class of scrips consisting of about 200 scrips. Market capitalization is one key factor in deciding which scrip should be classified in Group A.
"B" Group	Represents of two scrips "B1" which consists of scrips relatively liquid and with good track record. "B2" which consists of scrips with comparatively low liquidity.
"F" Group	Represents the fixed income securities
"G" Group	Represents trading in Government Securities by the retail investors
"T" Group	Represents scrips which are settled on a trade-to-trade basis as a surveillance measure
"Z" Group	Includes companies which have failed to comply with its listing requirements and/or have failed to resolve investor complaints and/or have not made the required arrangements with the Depositories, for dematerialization of their securities.

With effect from December 31, 2001, trading in all securities listed in equity in the Equity segment takes place in one market segment, viz., Compulsory Rolling Settlement (CRS) Segment.

The securities of companies which are in demat can be traded in market lot of 1. However, the securities of companies which are still in the physical form are traded in the market lot of generally either 50 or 100. Investors having quantities of securities less than the market lot are required to sell them as "Odd Lots". This facility offers an exit route to investors to dispose off their odd lots of securities, and also provides them an opportunity to consolidate their securities into market lots.

This facility of selling physical shares in compulsory demat scrips is called as Exit Route Scheme. This facility can also be used by small investors for selling up to 500 shares in physical form in respect of scrips of companies where trades are required to be compulsorily settled by all investors in demat mode.

BSE, in respect of securities of companies that are only listed/traded at BSE, considering their specific characteristics such a large number of companies, low to underrate market capitalization, lawyer contribution to overall trading turnover, classified equity securities of companies that are only listed/traded at BSE and satisfy certain paramount into separate sub-segments called "XC", "XD" and "XT". At the time of reviews any securities falling in Trade-for-Trade Segment (DT or "T" groups) are classified under "XT" sub-segments.

Computation of Closing Price of Scrips in the Cash Segment

The closing price of scrips is computed by the Exchange on the basis of weighted average price of all trades executed during the last 30 minutes of the continuous trading session. However, if there is no trade recorded during the last 30 minutes, then the last traded price of a scrip in the continuous trading session is taken as the official closing price.

BASKET TRADING SYSTEM

The Exchange commenced trading in the Derivatives Segment with effect from June 9, 2000 to enable the investors to, inter-alia, hedge their risks. Initially, the facility of trading in the Derivatives Segment was confined to Index Futures. Subsequently, the Exchange introduced the Index Options and Options & Futures in select individual stocks. The investors in cash market had felt a need to limit their risk exposure in the market to movement in Sensex.

With a view to provide investors the facility of creating Sensex linked portfolios and also to create a linkage of market prices of the underlying securities of Sensex in the Cash Segment and Futures on Sensex, the Exchange has provided to the investors as well its member-brokers, a facility of Basket Trading System on BOLT.

In the Basket Trading System :

- The investors through the member-brokers of the exchange are able to buy/sell all 30 scrips of Sensex in one go in the proportion of their respective weights in the Sensex.
- The investors can create their own baskets by deleting certain scrips from 30 scrips in the Sensex and also a place orders by entering value of Sensex portfolio to be bought or sold with a minimum value of 50,000/- for each order.
- The investors can alter the weights of securities in such profiled baskets and enter their own weights. The investors can also select less than 100% weightage to reduce the value of the basket as per their own requirements.
- To participate in this system, the member-brokers need to indicate number of Sensex basket(s) to be bought or sold, where the value of one Sensex basket is arrived at by the system by multiplying 50 to prevailing Sensex. Example: if the Sensex is 19,000, then value of one basket of Sensex would be $19,000 \times 50 = \text{i.e., } 9,50,000$.
- It provides the arbitrageurs an opportunity to take advantage of price differences in the underlying Sensex and Futures on the Sensex by simultaneous buying and selling of baskets comprising the Sensex scrips in the Cash Segment and Sensex Futures.
- It meets the need of investors and also improves the depth in cash and futures markets.

SETTLEMENT SYSTEM AT BSE**Compulsory Rolling Settlement**

All transactions in all groups of securities in the Equity segment and Fixed Income securities listed on BSE are required to be settled on T+2 basis (w.e.f. April 1, 2003). The settlement calendar, which indicates the dates of the various settlement related activities, is drawn by BSE in advance and is circulated among the market participants.

Under rolling settlements, the trades done on a particular day are settled after a given number of business days. A T+2 settlement cycle means that the final settlement of transactions done on T, i.e., trade day by exchange of monies and securities between the buyers and sellers respectively takes place on second business day (excluding Saturdays, Sundays, bank and Exchange trading holidays) after the trade day.

The transactions in securities of companies which have made arrangements for dematerialization of their securities are settled only in demat mode on T+2 on net basis, i.e., buy and sell positions of a member-broker in the same scrip are netted and the net quantity and value is required to be settled. However, transactions in securities of companies, which are in “Z” group or have been placed under “trade-to-trade” by BSE as a surveillance measure (“T”), are settled only on a gross basis and the facility of netting of buy and sell transactions in such scrips is not available.

The transaction in “F” group securities representing “Fixed Income Securities” and “G” group representing Government Securities for retail investors are also settled at BSE on T+2 basis.

Thus, the pay-in and pay-out of funds and securities takes places on the second business day (i.e., excluding Saturday, Sunday and bank & Exchange trading holidays) of the day of the execution of the trade.

The Information Systems Department of the Exchange generates, inter-alia, the following statements, which can be downloaded by the member-brokers in their back offices on a daily basis.

- (a) Statements giving details of the daily transactions entered into by the member-brokers.
- (b) Statements giving details of margins payable by the member-brokers in respect of the trades executed by them.
- (c) Statements of securities and fund obligation.
- (d) Delivery/Receive orders for delivery/receipt of securities.

The settlement of the trades (money and securities) done by a member-broker on his own account or on behalf of his individual, corporate or institutional clients may be either through the member-broker himself or through a SEBI registered custodian appointed by him/client. In case the delivery/payment in respect of a transaction executed by a member-broker is to be given or taken by a registered custodian, then the latter has to confirm the trade done by a member-broker on the BOLT System through 6A-7A entry. In case a transaction done by a member-broker is not confirmed by a registered custodian within the time permitted, the liability for pay-in of funds or securities in respect of the same devolves on the concerned member-broker.

6A/7A

A mechanism whereby the obligation of settling the transactions done by a member-broker on behalf of a client is passed on to a custodian based on confirmation of latter. The custodian can confirm the trades done by the member-brokers on-line and upto 11 a.m. on the next trading day. The late confirmation of transactions by the custodian after 11:00 a.m. upto 12:15 p.m., on the next trading day is, however, permitted subject to payment of charges for late confirmation @ 0.01% of the value of trades confirmed or ₹ 10,000/-, whichever is less.

Pay-in and Pay-out for 'A', 'B', 'T', 'C', 'F', 'G' & 'Z' group of securities

The trades done on BOLT by the Members in all securities in Compulsory rolling settlement (CRS) are now settled on BSE by payment of monies and delivery of securities on T+2 basis. All deliveries of securities are required to be routed through the Clearing House.

The Pay-in/Pay-out of funds based on the money statement and that of securities based on Delivery Order/ Receiver Order issued by BSE are settled on T+2 day.

Demat pay-in

The member-brokers can effect pay-in of demat securities to the Clearing House either through the National Securities Depository Ltd. (NSDL) or Central Depository Services (I) Ltd. (CDSL). In case of NSDL, the member-brokers are required to give instructions to their respective Depository Participants (DPs) specifying settlement no., settlement type, effective pay-in date, quantity, etc.

As regards CDSL, the member-brokers give pay-in instructions to their respective DPs. The securities are transferred by the DPs to the Clearing Member (CM) Principal Account. The member-brokers are required to give confirmation to their DPs, so that securities are processed towards pay-in obligations. Alternatively, the member-brokers may also effect pay-in from the clients' beneficiary accounts. For this, the clients are required to mention the settlement details and clearing member-broker ID of the member-broker through whom they have sold the securities. Thus, in such cases the Clearing Members are not required to give any delivery instructions from their accounts. In case a member fails to deliver the securities, the value of shares delivered short is recovered from him at the standard/closing rate of the scrips in the trading day.

Auto delivery facility

Instead of issuing Delivery instructions for their securities delivery obligations in demat mode in various scrips in a settlement /auction, a facility has been made available to the member-brokers of automatically generating Delivery instructions on their behalf from their CM Pool accounts maintained with NSDL and CM Principal Accounts maintained with CDSL. This auto delivery facility is available for CRS (Normal & Auction) and for trade to trade settlements. This facility is, however, not available for delivery of non-pari passu shares and shares having multiple International Securities Identification Number (ISINs). The member-brokers wishing to avail of this facility have to submit an authority letter to the Clearing House. This auto delivery facility is currently available for Clearing Member (CM) Pool accounts and Principal accounts maintained by the member-brokers with National Securities Depository Ltd. (NSDL) and Central Depositories Services (I) Ltd. (CDSL) respectively.

Pay-in of securities in physical form

In case of delivery of securities in physical form, the member-brokers have to deliver the securities to the Clearing House in special closed pouches along with the relevant details like distinctive numbers, scrip code, quantity, etc., on a floppy. The data submitted by the member-brokers on floppies is matched against the master file data on the Clearing House computer systems. If there is no discrepancy, then a scroll number is generated by the Clearing House and the securities are accepted.

Funds Pay-in

Once the reconciliation of securities is completed by the Clearing House, the bank accounts of member-brokers maintained with the ten clearing banks, are directly debited through computerized posting for their funds settlement obligations. Once the pay-in of securities and funds is complete, the Clearing House arranges for the pay-out of securities and funds.

In case of those members, whose funds pay-in obligations are returned by their clearing banks on account of insufficient funds in their bank accounts at the time of pay-in, their BOLT TWSs are now immediately de-activated during the trading hours itself, on receipt of such intimation from the clearing banks as against the earlier

practice of de-activating their BOLT TWSs at the end of trading on that day. BOLT TWSs of such members remain de-activated till the pay-in obligations are cleared by them.

Securities Pay-out

In case of demat securities, the same are credited by the Clearing House in the Pool/Principal Accounts of the member-brokers. The Exchange has also provided a facility to the member-brokers for transfer of pay-out securities directly to the clients' beneficiary owner accounts without routing the same through their Pool/Principal accounts in NSDL/CDSL. For this, the concerned member-brokers are required to give a client wise break up file which is uploaded by the member-brokers from their offices to the Clearing House. Based on the break up given by the member-brokers, the Clearing House instructs depositories, viz., CDSL & NSDL to credit the securities to the Beneficiary Owners (BO) Accounts of the clients. In case delivery of securities received from one depository is to be credited to an account in the other depository, the Clearing House does an inter depository transfer to give effect to such transfers.

In case of physical securities, the Receiving Members are required to collect the same from the Clearing House on the pay-out day.

This process of passing on delivery of securities purchased by the member-brokers to them by the Clearing House is called pay-out of securities.

Funds Payout

The bank accounts of the member-brokers having pay-out of funds are credited by the Clearing House with the Clearing Banks on the same day. This process is referred to as Pay-out of Funds.

In case, if a member-broker fails to deliver the securities, then the value of shares delivered short is recovered from him at the standard/closing rate of the scrips on the trading day.

In case of Rolling Settlements, pay-in and pay-out of both funds and securities, as stated earlier, is completed on the same day.

The settlement calendar, which indicates the dates of the various settlement related activities, is drawn by the Exchange in advance on a quarterly basis and is circulated among the market participants. The settlement calendars so drawn have been strictly adhered to by the Exchange and there has been generally no case of clubbing of settlements or postponement of pay-in and/ or pay-out during the last over seven years.

The Exchange maintains database of fake/forged, stolen, lost and duplicate securities in physical form with the Clearing House so that distinctive numbers submitted by member-brokers in case of physical securities on delivery may be matched against the database to weed out bad paper from circulation at the time of introduction of such securities in the market. This database has also been made available to the member-brokers so that both delivering and receiving member-brokers can check the entry of fake, forged and stolen shares in the market.

Surveillance at BSE

The main objective of the Surveillance function of the exchange is to promote market integrity in two ways:-

1. By monitoring price and volume movements (volatility) as well as by detecting potential market abuses at a nascent stage, and
2. By managing default risk by taking necessary actions timely.

All the instruments traded in the equity segment of Cash and Derivative market come under the Surveillance umbrella of BSE. Surveillance activities at the Exchange are divided broadly into two major segments, namely, price monitoring and position monitoring.

The detailed explanation of the various Surveillance activities are as follows :

(a) Price Monitoring

The functioning of the Price Monitoring is broadly divided into following activities:

- (i) On-Line Surveillance
- (ii) Off-Line Surveillance
- (iii) Derivative Market Surveillance
- (iv) Investigations
- (v) Surveillance Actions
- (vi) Rumour Verification
- (vii) Pro-active Measures

(i) On line Surveillance

One of the most important tools of the Surveillance is the On-line Real Time Surveillance system which was commissioned in 1999 with main objectives of detecting potential market abuses at a nascent stage to reduce the ability of the market participants to unduly influence the price and volumes of the scrips traded at the Exchange, improve the risk management system and strengthen the self regulatory mechanism at the Exchange.

The system has a facility to generate the alerts on-line, in real time, based on certain preset parameters like price and volume variations in scrips, members taking unduly large positions not commensurate with their financial position or having large concentrated position(s) in one or few scrips, etc.

(ii) Off-Line Surveillance

The Off-Line Surveillance system comprises of the various reports based on different parameters and scrutiny thereof.

- High/Low Difference in prices
- % change in prices over a week/fortnight/month
- Top N scrips by Turnover
- Trading in infrequently traded scrips
- Scrips hitting New High/Low

The Surveillance actions or investigations are initiated in the scrips identified from the above-stated reports.

(iii) Derivative Market Surveillance

Areas of Focus

- Abnormal fluctuation in the prices of a series
- Market Movement (Cash vis-a-vis Derivative)
- Member Concentration (Cash vis-a-vis Derivative)
- Closing Price Manipulation (Cash & Derivative)

(iv) Investigations

The Exchange conducts in-depth investigations based on preliminary enquiries/ analysis made into trading of the scrip as also at the instance of SEBI. In case irregularities observed, necessary actions are initiated and/or investigation case forwarded to SEBI, if necessary.

(v) Surveillance Actions*Special Margins*

Special margins are imposed on scrips which have witnessed abnormal price/ volume movements. Special margin is imposed @ 25 % or 50 % or 75 % as the case may be, on the client wise net outstanding purchase or sale position (or on both side) by the department.

Reduction of Circuit Filters

The circuit filters are reduced in case of illiquid scrips or as a price containment measure in low volume scrips. The circuit filters are reduced to 10 % or 5 % or 2 % as the case may be, based on the criteria decided by the Exchange.

Circuit Breakers

In addition to the price bands on individual scrips, SEBI decided to implement index based market wide circuit breakers system, w.e.f., July 02, 2001. The circuit breakers are applicable at three stages of the index movement either way at 10 %, 15 % and 20 %. These circuit breakers will bring about a coordinated trading halt in both Equity and Derivative market.

Trade to Trade

If a scrip is shifted on a Trade-to trade settlement basis, selling/ buying of shares in that scrip would result into giving/ taking delivery of shares at the gross level and no intra day/ settlement netting off/ square off facility would be permitted. The scrips which form part of 'Z group' are compulsorily settled on a trade to trade settlement basis. In addition to that Surveillance department transfers various scrips from time to time on a trade to trade settlement basis to contain the excessive volatility and/or abnormal volumes in the scrip.

Suspension of a scrip

The scrips are suspended by the Surveillance department in exceptional cases pending investigation or if the same scrip is suspended by any other Stock Exchange as a Surveillance action.

Warning to Members

The department may issue verbal/ written warning to member/s when market manipulation in the scrip is suspected.

Imposition of penalty/suspension/de-activation of terminals

The department imposes penalty or deactivate BOLT terminals or suspend the member/s who are involved in market manipulation, based on the input/ evidence available from investigation report or as and when directed by SEBI.

(vi) Rumour Verification

The following steps are involved in Rumour verification process:

- Surveillance Department liaises with Compliance Officers of companies to obtain comments of the company on various price sensitive corporate news items appearing in the selected News Papers.
- Comments received from the companies are disseminated to the Market by way of BOLT Ticker and/ or Notices in the Bulletin.
- Show cause notices are issued to companies which do not reply promptly to the Exchange.
- Investigations based on rumour verifications are carried out, if required, to detect cases of suspected insider trading

(vii) Pro-active Measures

- The Department compiled and disseminated a list of companies who have changed their names to suggest that their business interest is in the software Industry.
- List of NBFC's, whose application for registration rejected by RBI, was compiled and disseminated by the department.

(b) Position Monitoring

- (i) Statement of Top 100 Purchasers/Sellers
- (ii) Concentrated Purchases/Sales
- (iii) Purchases/Sales of Scrips having Thin Trading
- (iv) Trading in B1, B2 and Z group Scrips
- (v) Pay-in liabilities above a Threshold Limit
- (vi) Verification of Institutional Trades
- (vii) Snap Investigation
- (viii) Market Intelligence

The Surveillance Department closely monitors outstanding exposure of members on a daily basis. For this purpose, it has developed various off-line and on-line market monitoring reports. The reports are scrutinised to ascertain whether there is excessive purchase or sale position build up as compared to the normal business of the member, whether there are concentrated purchases or sales, whether the purchases have been made by inactive or financially weak members and even the quality of scrips is considered to assess the quality of exposure. Based on analysis of the above factors and the margins already paid and the capital deposited by the member, ad-hoc margins/early pay-in calls are made, if required. Some members are even advised to reduce their outstanding exposure in the market. Trading restrictions are placed on their business as and when deemed fit.

The department thus executes the Risk Management functions to avert possible payment default of members by taking timely corrective measures.

The following key areas are examined to assess the market risk involved.

(i) Statement of Top 100 Purchasers/Sellers

Statements of top 100 net purchasers and top 100 net sellers in case of A, B1, B2 and Z group of scrips are scrutinized, on a daily basis. This enables the Department to keep a watch on the exposure of the members, ascertain the quality of exposures, measure the risk vis-a-vis cover available by way of margins, capital etc. and initiate action such as imposition of ad-hoc margins, trading restriction etc. on the members.

A detailed report on the net outstanding positions of top purchasers and top sellers with exposures in individual scrips above certain limit, margin cover available etc., is prepared on a daily basis.

(ii) Concentrated Purchases/Sales

The concentration in purchases/sales of a member in a few scrips could be considered risky. In case, such a situation is noticed, fundamentals of the scrips, their daily turnover, their nature of transactions is ascertained. Thereafter, based on the market risk perception appropriate surveillance actions are taken.

(iii) Purchases/Sales of Scrips having Thin Trading

Purchases/sales by members in scrips having thin trading is closely scrutinised as comparatively high market risk is involved in trading in such scrips. Details of trades in such scrips are called from the members to assess the market risk involved and decide on the appropriate surveillance action.

(iv) Trading in B1, B2 and Z Group Scrips

The Exchange has classified the scrips listed on the Exchange into 'A', 'B1', 'B2' and 'Z' groups. In view of the price manipulation witnessed in a few B1, B2 and Z group scrips and also as a risk management measure, the Exchange has prescribed Exposure limits in B1, B2 and Z group scrips in a single Rolling Settlement.

(v) Pay-in liabilities of members above a threshold limit

The pay-in liability of members above a certain threshold limit is monitored with respect to the pay-in amount of the members, the members capital, the margin cover available to the Exchange against the members pay-in liability, etc. In case of inadequate margin cover, the reasons of the pay-in are ascertained. If warranted, advance pay-in is called to ensure that pay-in is completed smoothly.

(vi) Verification of Institutional Trade

The institutional trades executed by the member-brokers are verified to ascertain the genuineness of trades.

(vii) Snap Investigation

The Department also carries out, wherever considered necessary, preliminary investigation of certain dealings to verify irregularities. Further actions, viz., referring the case for detailed investigations, referring the cases to the Disciplinary Action Committee (DAC) of the Exchange for taking disciplinary action against members, referring cases to the Scrutiny Committee of the Exchange to re-assess the financial soundness of the members etc., are taken depending on the findings of preliminary investigation.

(viii) Market Intelligence

The rumours floating in the market are verified with the data available with the Exchange. Newspapers, Television news channels are referred to ascertain the national and global factors affecting the market sentiments. This enables the Exchange to avert market problems before it causes a serious damage.

On assessment of the market risk, decisions to call ad-hoc margins/early pay-in, advising the member to limit his business, summoning him for explanation, placing trading restriction, deactivation of BOLT TWS, etc. are taken.

Market Abuse

Market abuse is a broad term which includes abnormal price/ volume movement, artificial transactions, false or misleading impressions, insider trading, etc. In order to detect aberrant behaviour/ movement, it is necessary to know the normal market behaviour. The department uses various tools to determine normal and abnormal market behaviour. The necessary actions are initiated like imposition of special margin, reduction of circuit filters, trade to trade settlement, suspensions, de-activation of terminals, etc. to control abnormal market behaviour. The department carries out investigation, if necessary, based on the preliminary examination/analysis and suitable actions are taken against members involved based on the investigation.

NATIONAL STOCK EXCHANGE OF INDIA LTD. (NSEIL)

Based on Pherwani Committees report submitted in June, 1991, the National Stock Exchange of India Limited (NSEIL) was established to provide an efficient system eliminating all the deficiencies of stock exchanges and is geared to meet the requirements of the large investor population. It is a single stock exchange and all other centres are electronically linked to this exchange.

NSEIL was promoted by leading FIs at the behest of Government of India and was incorporated in November 1992 as a tax-paying company unlike other stock exchanges in the country. On its recognition as a stock exchange under the Securities Contracts (Regulation) Act, 1956 in April 1993, NSEIL commenced operations in the Wholesale Debt Market (WDM) segment in June 1994, operations in the Capital Market (CM) segment in November 1994, and operations in derivatives segment in June 2000.

Capital Market Segment

The Capital Market (CM) segment of NSEIL provides a fully automated screen based trading system for trading of equity and preference shares, debentures, warrants and coupons. The trading system, known as the National Exchange for Automated Trading (NEAT) system, is an anonymous order-driven system and operates on a strict price/time priority. It enables members from across the country to trade simultaneously with enormous ease and efficiency. It provides tremendous flexibility to the users in terms of kinds of orders that can be placed on the system. Several time-related (Good-till-Cancelled, Good-till-Day, Immediate-or-Cancel), price-related (buy/sell limit and stop-loss orders) or volume related (All-or-None, Minimum Fill, etc.) conditions can be easily built into an order. Orders are sorted and matched automatically by the computer keeping the system transparent, objective and fair. The trading system also provides complete market information on-line, which is updated on real time basis.

Wholesale Debt Market Segment

The WDM segment provides the only formal trading platform for trading of a wide range of debt securities. Initially, government securities, treasury bills and bonds issued by public sector undertakings (PSUs) were made available for trading. This range has been widened to include non-traditional instruments like floating rate bonds, zero coupon bonds, index bonds, commercial papers, certificates of deposit, corporate debentures, state government loans, SLR and non-SLR bonds issued by financial institutions, units of mutual funds and securitised debt.

The WDM trading system, known as NEAT (National Exchange for Automated Trading), is a fully automated screen based trading system that enables members across the country to trade simultaneously with enormous ease and efficiency. The trading system is an order driven system, which matches best buy and sell orders on a price/time priority.

Trading system provides two market sub-types: continuous market and negotiated market. In continuous market, the buyer and seller do not know each other and they put their best buy/sell orders, which are stored in order book with price/time priority. If orders match, it results into a trade. The trades in WDM segment are settled directly between the participants, who take an exposure to the settlement risk attached to any unknown counterparty.

In the negotiated market, the trades are normally decided by the seller and the buyer, and reported to the Exchange through the broker. Thus deals negotiated or structured outside the exchange are disclosed to the market through NEAT-WDM system. In negotiated market, as buyers and sellers know each other and have agreed to trade, no counter-party exposure limit needs to be invoked.

The trades on the WDM segment could be either outright trades or repo transactions with flexibility for varying days of settlement (T+0 to T+2) and repo periods (1 to 14 days). For every trade, it is necessary to specify the number of settlement days and the trade type (repo or non-repo) and in the event of a repo trade, the repo term.

The Futures and Option trading system, called NEAT-F&O trading system, provides a fully automated screen-based trading for S&P CNX Nifty futures on a nationwide basis and an online monitoring and surveillance mechanism.

The NEAT-F&O trading system is accessed by two types of users. The Trading Member (TM) has access to functions such as, order entry, order matching, order and trade management. The Clearing Member (CM) uses the trader workstation for the purpose of monitoring the trading member(s) for whom he clears the trades. Additionally, he can enter and set limits to position, which a trading member can take.

Contracts

Futures contract on the NSEIL is based on S&P CNX Nifty Index. Currently, it has a maximum of 3-month

expiration cycle. Three contracts are available for trading with 1 month, 2 months and 3 months expiry. A new contract is introduced on the next trading day following the expiry of the near month contract. Various conditions like, Good-till-Day, Good-till-Cancelled, Good-till- Date, Immediate or Cancel, Stop loss, etc. can be built into an order.

Clearing and Settlement

NSCCL undertakes clearing and settlement of all deals executed on the NSEIL's Derivatives segment. It acts as legal counterparty to all deals on the Derivatives segment and guarantees settlement.

Derivatives Segment

In the Derivatives segment, NSCCL has admitted Clearing Members (CMs) distinct from Trading Members (TMs) in line with the 2-tier membership structure stipulated by SEBI to enable wider participation in the Derivatives segment. All trades on the Derivatives segment are cleared through a CM of NSCCL.

Nifty index futures contracts are cash settled, i.e. through exchange of cash differences in value. Settlement is done on a daily basis by marking to market all open positions on the basis of the daily settlement price. The contracts are finally settled on expiry of the Nifty index futures contract when NSCCL marks the open positions of a CM to the closing price of the underlying index and resulting profit/loss is settled in cash.

TRADING AND SETTLEMENT AT NSE

NSE introduced for the first time in India, fully automated screen based trading. It uses a modern, fully computerised trading system designed to offer investors across the length and breadth of the country a safe and easy way to invest.

The NSE trading system called 'National Exchange for Automated Trading' (NEAT) is a fully automated screen based trading system, which adopts the principle of an order driven market.

National Securities Clearing Corporation Limited (NSCCL)

This company incorporated as a wholly owned subsidiary of the National Stock Exchange of India Limited carries out clearing and settlement of the trades executed in the capital market segment of National Stock Exchange. This company completes the settlement promptly without delay or deferment. It operates on behalf of the clearing members from and to regional clearing centres and central clearing centres at Mumbai. It was the first organisation to start pre-delivery verification to detect bad papers in the form of fake or forged certificates or lost and stolen share certificates through the automated mechanism of the clearing corporation. A facility is provided to lend/borrow securities as well as funds at market determined rates and enables timely delivery of securities with efficiency. This corporation is connected to National Securities Depository Limited (NSDL) and Central Depositories Services (India) Limited (CDSL) and carries out clearing and settlement services for other exchanges as well as for Index Futures.

Clearing Mechanism

Trades in rolling segment are cleared and settled on a netted basis. Trading and settlement periods are specified by the Exchange/Clearing Corporation from time to time. Deals executed during a particular trading period are netted at the end of that trading period and settlement obligations for that settlement period are computed. A multilateral netting procedure is adopted to determine the net settlement obligations.

In a rolling settlement, each trading day is considered as a trading period and trades executed during the day are netted to obtain the net obligations for the day.

Trade-for-trade deals and Limited Physical Market deals are settled on a trade for trade basis and settlement obligations arise out of every deal.

Clearing & Settlement (Equities)

NSCCL carries out clearing and settlement functions as per the settlement cycles of different sub-segments in the Equities segment.

The clearing function of the clearing corporation is designed to work out a) what counter parties owe and b) what counter parties are due to receive on the settlement date. Settlement is a two way process which involves legal transfer of title to funds and securities or other assets on the settlement date.

NSCCL has also devised mechanism to handle various exceptional situations like security shortages, bad delivery, company objections, auction settlement etc.

NSCCL has empanelled 8 clearing banks to provide banking services to trading members and has established connectivity with both the depositories for electronic settlement of securities.

Clearing

Clearing is the process of determination of obligations, after which the obligations are discharged by settlement.

NSCCL has two categories of clearing members: trading members and custodians. The trading members can pass on its obligation to the custodians if the custodian confirms the same to NSCCL. All the trades whose obligation the trading member proposes to pass on to the custodian are forwarded to the custodian by NSCCL for their confirmation. The custodian is required to confirm these trade on T + 1 days basis.

Once, the above activities are completed, NSCCL starts its function of Clearing. It uses the concept of multi-lateral netting for determining the obligations of counter parties. Accordingly, a clearing member would have either pay-in or pay-out obligations for funds and securities separately. Thus, members pay-in and pay-out obligations for funds and securities are determined latest by T + 1 day and are forwarded to them so that they can settle their obligations on the settlement day (T+2).

Cleared and non-cleared deals

NSCCL carries out the clearing and settlement of trades executed in the following sub-segments of the Equities segment:

1. All trades executed in the Book entry/Rolling segment.
2. All trades executed in the Limited Physical Market segment.

NSCCL does not undertake clearing and settlement of deals executed in the Trade for Trade sub-segment of the Equities (Capital Market) segment of the Exchange. Primary responsibility of settling these deals rests directly with the members and the Exchange only monitors the settlement. The parties are required to report settlement of these deals to the Exchange.

Trading in Retail Debt Segment

Trading in the Retail Debt Market takes place in the same manner in which the trading takes place in the equities (Capital Market) segment. The RETDEBT Market facility on the NEAT system of Capital Market Segment is used for entering transactions in RDM session.

Members eligible for trading in RDM segment

Trading Members who are registered members of NSE in the Capital Market segment and Wholesale Debt Market segment are allowed to trade in Retail Debt Market (RDM) subject to fulfilling the capital adequacy norms.

Trading Members with membership in Wholesale Debt Market segment only, can participate in RDM on submission of a letter in the prescribed format

Trading System

Trading in RDM also take place on the 'National Exchange for Automated Trading' (NEAT) system, a fully automated screen based trading system, which adopts the principle of an order driven market. The RETDEBT Market facility on the NEAT system of Capital Market Segment is used for entering transactions in RDM session.

The securities available in this segment will not available in F & O and inquiry terminal.

Trading Cycle

Trading in Retail Debt Market is permitted under Rolling Settlement, where in each trading day is considered as a trading period and trades executed during the day are settled based on the net obligations for the day.

Settlement is on a T+2 basis i.e. on the 2nd working day. For arriving at the settlement day all intervening holidays, which include bank holidays, NSE holidays, Saturdays and Sundays are excluded. Typically trades taking place on Monday are settled on Wednesday, Tuesday's trades settled on Thursday and so on.

Settlement

Primary responsibility of settling trades concluded in the WDM segment rests directly with the participants and the Exchange monitors the settlement. Mostly these trades are settled in Mumbai. Trades are settled gross, i.e. on trade for trade basis directly between the constituents/participants to the trade and not through any Clearing House mechanism. Thus, each transaction is settled individually and netting of transactions is not allowed.

Settlement is on a rolling basis, i.e. there is no account period settlement. Each order has a unique settlement date specified upfront at the time of order entry and used as a matching parameter. It is mandatory for trades to be settled on the predefined settlement date. The Exchange currently allows settlement periods ranging from same day (T+0) settlement to a maximum of (T+2).

On the scheduled settlement date, the Exchange provides data/information to the respective member/participant regarding trades to be settled on that day with details like security, counter party and consideration.

The participants through their Subsidiary General Ledger (SGL) account (a book entry settlement system) settle government securities including treasury bills with RBI or through exchange of physical certificates. Other instruments are settled through delivery of physical securities.

Where trade is settled through the SGL account, exchange of securities and funds is done on DVP basis. Where trade is settled through delivery of certificates, the consideration is paid through cheque, payorder, Banker's cheque or RBI cheque.

The required settlement details, i.e. certificate no., SGL form no., Cheque no., constituent etc. are reported by the member/participant to the Exchange.

The Exchange closely monitors the settlement of transactions through the reporting of settlement details by members and participants. In case of deferment of settlement or cancellation of trade, participants are required to seek prior approval from the Exchange. For any dispute arising in respect of the trades or settlement, the exchange has established arbitration mechanism for resolving the same.

STRAIGHT THROUGH PROCESSING

The global securities market is passing through an interesting phase. Driven by globalization of the securities market, technology innovations and increasing trade volumes, the financial industry is moving towards Straight Through Processing.

Straight Through Processing (STP) is generally understood to be a mechanism that automates the end to end processing of transactions of financial instruments. It involves use of a system to process or control all elements

of the work flow of a financial transaction, what are commonly known as the Front, Middle, Back office and General Ledger. In other words, STP allows electronic capturing and processing of transactions in one pass from the point of order origination to final settlement.

STP thus streamlines the process of trade execution and settlement and avoids manual entry and re-entry of the details of the same trade by different market intermediaries and participants. Usage of STP enables orders to be processed, confirmed, settled in a shorter time period and in a more cost effective manner with fewer errors.

Advantages of Straight Through Processing

Advantages of Straight through Processing as under:

- Reduced risk
- Automation of manual process minimizing errors
- Improved operational efficiency in handling larger volumes
- Facilitates movement towards shorter settlement cycles (T+1)
- Lower cost per trade
- Timely settlement of trades and instructions
- Eliminates paper work and minimizes manual intervention
- Enables increased cross border trading (FII trades)
- Greater transparency with clear audit trail
- Increases competitive advantage of our markets
- Messaging standards as per ISO 15022 standards

Straight Through Processing (STP) thus aims to bring in non-duplication of work, efficiency and automation of the manual procedures right from trade initiation to settlement processes.

SEBI had mandated the use of Straight Through Processing (STP) system for all institutional trades w.e.f. July, 2004. In order to regulate the STP service it had also issued SEBI (STP Centralised Hub and STP Service Providers) Guidelines, 2004 (STP Guidelines) which also prescribes the model agreement between the STP centralised hub and the STP service providers.

STP guidelines prescribes the eligibility criteria and conditions of approval for the STP centralised hub and the STP service providers, obligations and responsibilities of the STP centralised hub and the STP service providers and code of conduct for the STP service providers. The STP centralised hub and the STP service providers are required to abide by these Guidelines. To prescribe contractual obligations between the STP centralised hub and the STP service providers and to facilitate standardisation of service, a model agreement between the STP centralised hub and the STP service providers has also been prescribed by SEBI as Schedule II to the Guidelines. The agreement between the STP centralised hub and the STP service provider includes the provisions included in the model agreement.

DIRECT MARKET ACCESS (DMA)

Direct Market Access (DMA) is a facility which allows brokers to offer clients direct access to the exchange trading system through the broker's infrastructure without manual intervention by the broker. Some of the advantages offered by DMA are direct control of clients over orders, faster execution of client orders, reduced risk of errors associated with manual order entry, greater transparency, increased liquidity, lower impact costs for large orders, better audit trails and better use of hedging and arbitrage opportunities through the use of decision support tools / algorithms for trading.

While ensuring conformity with the provisions of the Securities Contract (Regulations) Act, 1956, Stock Exchanges may facilitate Direct Market Access for investors subject to the following conditions:

1. Application for Direct Market Access (DMA) facility

Brokers interested to offer DMA facility shall apply to the respective stock exchanges giving details of the software and systems proposed to be used, which shall be duly certified by a Security Auditor as reliable.

The stock exchange should grant approval or reject the application as the case may be, and communicate its decision to the member within 30 calendar days of the date of completed application submitted to the exchange.

The stock exchange, before giving permission to brokers to offer DMA facility shall ensure the fulfillment of the conditions specified in this circular.

2. Operational specifications

All DMA orders shall be routed to the exchange trading system through the broker's trading system. The broker's server routing DMA orders to the exchange trading system shall be located in India. The broker should ensure sound audit trail for all DMA orders and trades, and be able to provide identification of actual user-id for all such orders and trades. The audit trail data should be available for at least 5 years. Exchanges shall maintain statistical data on DMA trades and provide information on the same to SEBI on a need basis. The DMA system shall have sufficient security features including password protection for the user ID, automatic expiry of passwords at the end of a reasonable duration, and reinitialisation of access on entering fresh passwords. Brokers should follow the similar logic/priorities used by the Exchange to treat DMA client orders. Brokers should maintain all activities/alerts log with audit trail facility. The DMA Server should have internally generated unique numbering for all such client order/trades. A systems audit of the DMA systems and software shall be periodically carried out by the broker as may be specified by the exchange and certificate in this regard shall be submitted to the exchange. The exchanges and brokers should provide for adequate systems and procedures to handle the DMA trades.

3. Client Authorization and Broker – Client agreement

Exchanges shall specify from time to time the categories of investors to whom the DMA facility can be extended. Initially, the permission is restricted to institutional clients. Brokers shall specifically authorize clients for providing DMA facility after fulfilling Know Your Client requirements and carrying out due diligence regarding clients' credit worthiness, risk taking ability, track record of compliance and financial soundness. Brokers shall ensure that only those clients who are deemed fit and proper for this facility are allowed access to the DMA facility. Brokers shall maintain proper records of such due diligence. Individual users at the client end shall also be authorized by the broker based on minimum criteria. The records of user details, user-id and such authorization shall be maintained by the broker. Details of all user-ids activated for DMA shall be provided by the broker to the exchange.

The broker shall enter into a specific agreement with the clients for whom they permit DMA facility. This agreement will include the following safeguards:

- (a) The client shall use the DMA facility only to execute his own trades and shall not use it for transactions on behalf of any other person / entity.
- (b) Electronic/Automated Risk management at the broker's level before release of order to the Exchange system. The client shall agree to be bound by the various limits that the broker shall impose for usage of the DMA facility.
- (c) Right to withdraw DMA facility if the limits set up are breached or for any other such concerns
- (d) Withdrawal of DMA facility on account of any misuse or on instructions from SEBI/Exchange.

Exchanges shall prepare a model agreement for this purpose. The broker's agreement with clients should not have any clause that is less stringent/contrary to the conditions stipulated in the model agreement

4. Risk Management

The broker shall ensure that trading limits/ exposure limits/ position limits are set for all DMA clients based on risk assessment, credit quality and available margins of the client. The broker system shall have appropriate authority levels to ensure that the limits can be set up only by persons authorized by the risk / compliance manager. The broker shall ensure that all DMA orders are routed through electronic/automated risk management systems of the broker to carry out appropriate validations of all risk parameters including Quantity Limits, Price Range Checks, Order Value, and Credit Checks before the orders are released to the Exchange.

All DMA orders shall be subjected to the following limits:

- (a) Order quantity / order value limit in terms of price and quantity specified for the client.
- (b) All the position limits which are specified in the derivatives segment as applicable.
- (c) Net position that can be outstanding so as to fully cover the risk emanating from the trades with the available margins of the specific client.
- (d) Appropriate limits for securities which are subject to FII limits as specified by RBI.

The broker may provide for additional risk management parameters as they may consider appropriate.

5. Broker to be liable for DMA trades

The broker shall be fully responsible and liable for all orders emanating through their DMA systems. It shall be the responsibility of the broker to ensure that only clients who fulfill the eligibility criteria are permitted to use the DMA facility

6. Cross Trades

Brokers using DMA facility for routing client orders shall not be allowed to cross trades of their clients with each other. All orders must be offered to the market for matching.

7. Other legal provisions

In addition to the requirements mentioned above, all existing obligations of the broker as per current regulations and circulars will continue without change. Exchanges may also like to specify additional safeguards / conditions as they may deem fit for allowing DMA facilities to their brokers.

DEMUTUALIZATION OF STOCK EXCHANGES

The process of demutualization is to convert the traditional “not for-profit” stock exchanges into a “for profit” company and this process is to transform the legal structure from a mutual form to a business corporation form. SEBI had set up a committee under the Chairmanship of Justice Kania for the same which came up with report on demutualization of Stock Exchanges through uniform scheme prescribed. Accordingly, SEBI issued scheme of demutualization to BSE and other Regional Stock Exchanges.

The important features of the demutualisation exercise are as follows :

- (1) The board of a stock exchange should consist of 75% public interest/ shareholder directors and only 25% broker directors, and
- (2) 51% shareholding of the stock exchange should be divested to public/ investors other than trading member brokers and only 49% of shareholding can remain with the trading member brokers. This will transform our broker-owned stock exchanges into professionally-run corporate stock exchanges.

The options prescribed for divestment/dilution of brokers’ shareholding in a stock exchange are as follows:

- (1) Offer for sale, by issue of prospectus, of shares held by trading member brokers.
- (2) Private placement of shares (either of the shares held by the member brokers or new shares by the exchange) to any person or group of persons subject to the prior approval of SEBI and the maximum limit of 5% to any single person/group of persons.
- (3) Fresh issue of shares to the public through an IPO.

The purpose of demutualisation is as follows:

1. Stock exchanges owned by members tend to work towards the interest of members alone, which could on occasion be detrimental to rights of other stakeholders. Division of ownership between members and outsiders can lead to a balanced approach, remove conflicts of interest, create greater management accountability.
2. Publicly owned stock exchanges can enter into capital market for expansion of business.
3. Publicly owned stock exchange would be more professionally managed than broker owned.
4. Demutualisation enhances the flexibility of management.

SMALL AND MEDIUM ENTERPRISE (SME) EXCHANGE

SME exchange means a trading platform of a recognised stock exchange having nationwide trading terminals permitted by SEBI to list the specified securities issued in accordance with SEBI (ICDR) Regulation and includes a stock exchange granted recognition for this purpose but does not include the Main Board.

Here Main Board means a recognized stock exchange having nationwide trading terminals, other than SME exchange.

The two stock exchange of India i.e. Bombay Stock Exchange (BSE) and National Stock Exchange (NSE) have begun their SME listing platforms. While BSE SME Exchange began its operation in March, 2012, NSE's SME exchange titled EMERGE commenced operations in September, 2012.

Benefits of Listing on SME Exchange

- Access to capital and future financing opportunities
- Going public would provide the MSME's with equity financing opportunities to grow their business - from expansion of operations to acquisitions.
- Companies in the growth phase tend to get over-leveraged at which point, banks are reluctant to provide further credit. Equity capital is then necessary to bring back strength to the balance sheet. The option of equity financing through the equity market allows the firm to not only raise long-term capital but also get further credit due through an additional equity infusion. The issuance of public shares expands the investor base, and this in turn will help set the stage for secondary equity financings, including private placements.
- In addition, Issuers often receive more favourable lending terms when borrowing from financial institutions. The mechanics of listing on a stock exchange (audited balance sheets, being subject to corporate governance norms etc) would address many of the transparency and informational asymmetry constraints that the financial institutions face in lending to the SME sector. In addition, equity financing lowers the debt burden leading to lower financing costs and healthier balance sheets for the firms. The continuing requirement for adhering to the stock market rules for the issuers lower the on-going information and monitoring costs for the banks.

- *Increased visibility and prestige*

Going public is likely to enhance the company's visibility. Greater public awareness gained through media coverage, publicly filed documents and coverage of stock by sector investment analysts can provide the SME with greater profile and credibility. This can result in a more diversified group of investors, which may increase the demand for that company's shares leading to an increase in the company's value.

- *Venture Capital (VC)*

It has been seen that there is greater vitality of venture capital in stock market centered systems. The underdeveloped equity culture has made it difficult for companies to both get into the VC phase as well as graduate from venture capital/startups phase to a scale of operations that would make them internationally competitive. A vibrant equity market would provide prove to be an added incentive for greater venture capital participation by providing an exit option leading to a reduction in their lock-in period.

- *Liquidity for shareholders*

Becoming a public company establishes a market for the company's shares, providing its investors with an efficient and regulated vehicle in which to trade their own shares. Greater liquidity in the public market can lead to better valuation for shares than would be seen through private transactions.

- *Create employee incentive mechanisms*

The employees of the SME enterprises can participate in the ownership of their own company and benefit from being a shareholder. This can serve to ensure stronger employee commitment to the company's performance and success. Share options in a public company have an immediate and tangible value to employees, especially as a recruitment incentive.

- *Facilitate growth through Mergers and Acquisitions*

As a public company, company's shares can be utilized as an acquisition currency to acquire target companies, instead of a direct cash offering. Using shares for an acquisition can be a tax efficient and cost effective vehicle to finance such a transaction.

- *Encourages Innovation & Entrepreneurial Spirit*

The ability of companies in their early stages of development to raise funds in the capital markets allows these companies to grow very quickly. This growth helps speed up the dissemination of new technologies throughout the economy. In addition, by raising the returns available from pursuing new ideas, technologies etc the capital markets facilitate entrepreneurial activities.

- *Efficient Risk Distribution*

The development of the capital markets has helped distribute risk more efficiently by transfer of risk to those best able to bear it. This ability to transfer risk facilitates greater risk- taking, but this increased risk-taking does not destabilize the economy. Thus the capital markets ensure that capital flows to its best uses and that riskier activity with higher payoffs are funded.

Institutional Trading Platform (ITP)

SEBI has notified new norms for listing of small and medium enterprises (SMEs) including the start-up companies on Institutional Trading Platform (ITP) on stock exchanges without an initial public offering. This will allow SMEs to list themselves on stock exchanges without raising funds from the public, which in turn will help both the investor and the small companies.

In the modified rules to permit listing of start-ups and SMEs in ITP without having to make an IPO, a minimum amount for trading or investment on the ITP would be Rs. 10 lakh. This move will provide easier exit options for entities such as Angel Investors, Venture Capital Funds and Private Equities. Besides, the move would provide better visibility, wider investor base and greater fund raising capabilities to such companies. SEBI notified that the company would not make an IPO while its specified securities are listed on ITP, but can raise capital through private placement or rights issue without an option for renunciation of rights. An SME will be eligible to list on the ITP, in case the company, its promoter, director, Group Company does not appear in the defaulters list of Reserve Bank and there is no winding up petition against the firm.

Dedicated Debt Segment on Stock Exchanges

SEBI vide circular dated January 24, 2013 prescribed guidelines for providing dedicated debt segment on stock exchanges. Further, SEBI vide circular dated September 12, 2013 prescribed the Risk Management Framework for Dedicated Debt Segment on Stock Exchanges. The debt segment shall offer separate trading, clearing, settlement, reporting facilities and membership to deal in :

- (i) “debt securities” as defined in Securities and Exchange Board of India (Issue and Listing of Debt Securities) Regulations, 2008;
- (ii) Government Securities, Treasury Bills, State Government loans, SLR and Non-SLR Bonds issued by Financial Institutions, municipal bonds, single bond repos, basket repos and CBLO kind of products subject to RBI approval, where required;
- (iii) Securitised debt instruments as defined in SEBI (Public Offer and Listing of Securitised Debt Instruments) Regulations, 2008;
- (iv) any other debt instruments as may be specified from time to time by the competent authority.

ALGORITHMIC TRADING

Any order that is generated using automated execution logic shall be known as algorithmic trading.

With the increasing trend amongst capital market players of generating orders through automated execution logic called Algorithmic Trading. SEBI have formulated broad guidelines to be followed by both Stock Exchanges and Stock Brokers for Algorithmic Trading. These guidelines permits secure systems for algorithmic trading and help to keep pace with the speed of trade and volume of data that may arise through it.

Broadly the Guidelines provides the following directions :

- The stock brokers / trading members that provide the facility of algorithmic trading shall subject to their algorithmic trading system to a system audit every six months in order to ensure that the requirements prescribed by SEBI / stock exchanges with regard to algorithmic trading are effectively implemented.
- Such system audit of algorithmic trading system shall be undertaken by a system auditor who possess any of the following certifications:
 - (a) CISA (Certified Information System Auditors) from ISACA;
 - (b) DISA (Post Qualification Certification in Information Systems Audit) from Institute of Chartered Accountants of India (ICAI);
 - (c) CISM (Certified Information Securities Manager) from ISACA;
 - (d) CISSP (Certified Information Systems Security Professional) from International Information Systems Security Certification Consortium, commonly known as (ISC).
- Deficiencies or issues identified during the process of system audit of trading algorithm / software shall be reported by the stock broker / trading member to the stock exchange immediately on completion of

the system audit. Further, the stock broker / trading member shall take immediate corrective actions to rectify such deficiencies / issues.

- In case of serious deficiencies / issues or failure of the stock broker / trading member to take satisfactory corrective action, the stock exchange shall not allow the stock broker / trading member to use the trading software till deficiencies / issues with the trading software are rectified and a satisfactory system audit report is submitted to the stock exchange. Stock exchanges may also consider imposing suitable penalties in case of failure of the stock broker / trading member to take satisfactory corrective action to its system within the time-period specified by the stock exchanges.
- Stock exchanges shall periodically review their surveillance arrangements in order to better detect and investigate market manipulation and market disruptions.
- The penalty rates specified by the stock exchanges of 'charges to be levied per algo orders' are required to be double.
- In order to discourage repetitive instances of high daily order-to-trade ratio, stock exchanges shall impose an additional penalty in form of suspension of proprietary trading right of the stock broker / trading member for the first trading hour on the next trading day in case a stock broker / trading member is penalized for maintaining high daily order-to-trade ratio, provided penalty was imposed on the stock broker / trading member on more than ten occasions in the previous thirty trading days.

LESSON ROUND UP

- Securities traded in the stock exchanges can be classified as Listed cleared Securities and Permitted Securities.
- Settlement is the process of netting of transactions and actual delivery/receipt of securities and transfer deeds against receipts/payment of agreed amount.
- National Securities Clearing Corporation Limited incorporated as a wholly owned subsidiary of the National Stock Exchange of India Limited carries out clearing and settlement of the trades executed in the capital market segment of National Stock Exchange.
- The member-brokers at BSE &NSE now enter orders for purchase or sell of securities from Trader Work Stations (TWSs) through BOLT and NEAT system.
- Securities lending is a scheme under which a person with idle shares can lend them to another who does not have the shares to fulfill his obligation under a trade finalized by him.
- Straight Through Processing (STP) is a mechanism that automates the end to end processing of transactions of financial instruments.
- Direct Market Access (DMA) is a facility which allow brokers to offer clients direct access to the exchange trading system through the broker's infrastructure without manual intervention by the broker.
- With the increasing trend amongst capital market players of generating orders through automated execution logic called Algorithmic Trading.
- SME exchange means a trading platform of a recognised stock exchange having nationwide trading terminals permitted by SEBI to list the specified securities issued in accordance with SEBI (ICDR) Regulation, 2009 and includes a stock exchange granted recognition for this purpose but does not include the Main Board.
- An order that is generated using automated execution . Logic shall be known as algorithmic trading.

GLOSSARY

Bear Market	A weak or falling market characterized by the dominance of sellers.
Bull Market	A rising market with abundance of buyers and relatively few sellers.
Cash Market	A market for sale of security against immediate delivery, as opposed to the futures market.
Clearing	Settlement or clearance of accounts, for a fixed period in a Stock Exchange.
Daily Margin	The amount that has to be deposited at the Stock Exchange on a daily basis for the purchase or sale of a security. This amount is decided by the stock exchange.
Jobber	Member brokers of a stock exchange who specialize, by giving two way quotations, in buying and selling of securities from and to fellow members. Jobbers do not have any direct contact with the public but they serve the useful function of imparting liquidity to the market.

SELF TEST QUESTIONS

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation.)

1. What is a SME Exchange? What are the benefits available to accompany on listing at SME exchange?
2. Discuss the procedure for settlement of securities under rolling settlement.
3. Discuss the framework for securities lending and borrowing.
4. What is straight through processing? What are its advantages?
5. Briefly explain about Direct Market Access.
6. What is Algorithmic Trading? Enumerate the guidelines prescribed by SEBI for Stock Broker in this behalf?
7. What is 'demutualization' of stock exchange? Briefly discuss the important features of demutualization of stock exchange.

Lesson 5

Debt Market

LESSON OUTLINE

- Introduction
- Debt Market Instruments
- Corporate Debenture
- Fixed Income Products
- Interest Based Bonds
- Derived Instruments
- Bench Marked Instruments
- Investors in Debt Market
- Debt Market Intermediaries/Participants
- Debt Market in India – Regulatory Framework
- SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009
- SEBI (Issue and Listing of Debt Securities) Regulations, 2008
- SEBI (Public Offer and Listing of Securitised Debt Instruments) Regulations, 2008
- Municipal Bonds
- SEBI (Issue and Listing of Debt Securities by Municipality) Regulations, 2015
- Compliance under SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015
- LESSON ROUND UP
- GLOSSARY
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

Debt Market are market for issuance, trading and settlement of various types and features of fixed income securities.

A vibrant debt market enables investors to shuffle and reshuffle their portfolio depending upon the expected changes. A well functioning debt market becomes significant for all the market participants. The debt market in India comprises broadly of two segments, viz., Government Securities Market and Corporate Debt Market.

In this lesson the significance of debt market in general and its role in accelerating the development of economic growth in particular, Development of Debt Market in India, the policies initiated by Securities and Exchange Board of India, instruments, investors, participants, issuers and intermediaries available in the Debt market, Regulatory Framework for issue of debt securities, Municipal Bonds and SEBI Regulation with respect to Municipal Bonds and Compliance under SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, etc., are explained.

INTRODUCTION

Debt markets are markets for the issuance, trading and settlement of various types and features of fixed income securities. Fixed income securities can be issued by any legal entity like central and state governments, public bodies, statutory corporations, banks and institutions and corporate bodies.

The debt market in India comprises mainly of two segments viz., the Government securities market consisting of Central and State Governments securities, Zero Coupon Bonds (ZCBs), Floating Rate Bonds (FRBs), T-Bills and the corporate securities market consisting of FI bonds, PSU bonds, and Debentures/Corporate bonds. Government securities form the major part of the market in terms of outstanding issues, market capitalization and trading value.

The trading of government securities on the Stock exchanges is currently through Negotiated Dealing System using members of Bombay Stock Exchange (BSE) / National Stock Exchange (NSE) and these trades are required to be reported to the exchange. The bulk of the corporate bonds, being privately placed, were, however, not listed on the stock exchanges. Two Depositories, National Securities Depository Limited (NSDL) and Central Depository Services (India) Limited (CDSL) maintain records of holding of securities in a dematerialized form. Records of holding of government securities for wholesale dealers like banks/Primary Dealers (PDs) and other financial institutions are maintained by the RBI.

Negotiated Dealing System (NDS) is an electronic platform for facilitating dealing in Government Securities and Money Market Instruments. NDS facilitates electronic submission of bids/application by members for primary issuance of Government Securities by RBI through auction and floatation. It will provide an interface to the Securities Settlement System.

DEBT MARKET INSTRUMENTS

CORPORATE DEBENTURE

It is a debt security issued by a company, which offers to pay interest in lieu of the money borrowed for a certain period. In essence it represents a loan taken by the issuer who pays an agreed rate of interest during the lifetime of the instrument and repays the principal normally, unless otherwise agreed, on maturity.

These are long-term debt instruments issued by private sector companies, in denominations as low as ₹ 1000 and have maturities ranging between one and ten years. Debentures enable investors to reap the dual benefits of adequate security and good returns. Unlike other fixed income instruments such as Fixed Deposits, Bank Deposits, Debentures can be transferred from one party to another.

Debentures can be divided into different categories on the basis of convertibility of the instrument and Security.

The debentures issued on the basis of Security includes –

- Non-Convertible Debentures (NCDs)
- Partly Convertible Debentures (PCDs)
- Fully convertible Debentures (FCDs)
- Optionally Convertible Debentures (OCDs)
- Secured Debentures
- Unsecured Debentures

FIXED INCOME PRODUCTS

Deposit	It serve as medium of saving and as a means of payment and a bank basically has three types of deposits, i.e. time deposit, savings deposit and current account.
Fixed Deposit	Fixed Deposits are sums accepted by most of the NBFCs and banks for certain point of time. However, the interest rate offered by NBFC is regulated by RBI. The deposits offered by NBFCs are not insured whereas the deposits accepted by most banks are insured up to a maximum of Rs.1, 00,000.

INTEREST BASED BONDS

Coupon Bonds	Coupon Bonds pays periodic interest at the pre-determined rate of interest. The annual rate at which the interest is paid is known as the coupon rate or simply the coupon. The dates on which the interest payments are made, are known as the coupon due dates. Interest is usually paid half-yearly though in some cases it may be monthly, quarterly, annually or at some other periodicity
Zero Coupon Bonds	A zero coupon bond does not carry any coupon and are issued at a discount to its face value. Gain to the investor is difference between the issue price and the face value of bonds.

DERIVED INSTRUMENTS

These instruments are not direct debt instruments. Instead they derive value from various debt instruments. The following are the derived instruments:

Mortgage Bonds	Mortgage backed bonds is a collateralized term-debt offering. Every issue of such bonds is backed by a pledged collateral. These bonds are like the bonds floated in the capital market, semi-annual or quarterly payments of interest and final bullet payment of principal.
Pass through Certificates	When mortgages are pooled together and undivided interest in the pool are sold. It promises that the cash flow from the underlying mortgages would be passed through to the holders of the securities in the form of monthly payments of interest and principal.
Participation Certificates	These are strictly inter-bank instruments confined to the scheduled commercial banks and its tenure does not exceeding 90 days. Interests rate on such certificate are determined by the two contracting banks.

BENCHMARKED INSTRUMENTS

An Instrument in which the payment of interest is based on some benchmark index is known as benchmark instruments. The following are the benchmarked instruments:

Floating Interest Rate	Interest rate is not fixed and periodically the interest rate payable for the next period is set with reference benchmarked Index such as LIBOR, MIBOR, etc.
Inflation Linked Bonds	In these bonds, payments are indexed by reference to the change in the value of a general price or wage index over the term of the instrument. The options are that either the interest payments are adjusted for inflation or the principal repayment or both.

INVESTORS IN DEBT MARKET

Investors are the entities who invest in fixed income instruments. The investors in such instruments are generally Banks, Financial Institutions, Mutual Funds, Insurance Companies, Provident Funds etc. The individual investors invest to a great extent in Fixed Income products.

Banks

Collectively all the banks put together are the largest investors in the debt market. They invest in all instruments ranging from T-Bills, CPs and CDs to GOISECs, private sector debentures etc. Banks lend to corporate sector directly by way of loans and advances and also invest in debentures issued by the private corporate sector and in PSU bonds.

Insurance Companies

The second largest category of investors in the debt market are the insurance companies.

Provident Funds

Provident funds are estimated to be the third largest investors in the debt market. Investment guidelines for provident funds are being progressively liberalized and investment in private sector debentures is one step in this direction.

Most of the provident funds are very safety oriented and tend to give much more weightage to investment in government securities although they have been considerable investors in PSU bonds as well as state government backed issues.

Mutual Funds

Mutual funds represent an extremely important category of investors. World over, they have almost surpassed banks as the largest direct collector of primary savings from retail investors. Mutual funds include the Unit Trust of India, the mutual funds set up by nationalized banks and insurance companies as well as the private sector mutual funds set up by corporates and overseas mutual fund companies.

Trusts

Trusts include religious and charitable trusts as well as statutory trusts formed by the government and quasi government bodies. There are very few instruments in which trusts are allowed to invest. Most of the trusts invest in CDs of banks and bonds of financial institutions and units of Unit Trust of India.

Corporate Treasuries

Corporate Treasuries have become prominent investors only in the last few years. Treasuries could be either those of the public sector units or private sector companies or any other government bodies or agencies. The treasuries of PSUs as well as the governmental bodies are allowed to invest in papers issued by DFIs and banks as well as GOISECs of various maturities. However the orientation of the investments is mostly in short-term instruments or sometimes in extremely liquid long term instruments which can be sold immediately in the markets.

In complete contrast to public sector treasuries, those in the private sector invest in CDs of banks and CPs of other private sector companies, GOISECs as well as debentures of other private sector companies.

Foreign Portfolio Investors (FPIs)

India does not allow capital account convertibility either to overseas investors or to domestic residents. Registered FPIs are exception to this rule. FPIs have to be specifically and separately approved by SEBI for equity and

debt. Each FPIs is allocated a limit every year up to which it can invest in Indian debt securities. They are also free to disinvest any of their holdings, at any point of time, without prior permission.

Retail Investors

Since January 2002, retail investors have been permitted to submit non-competitive bids at primary auction through any bank or Primary Dealers (PDs).

DEBT MARKET INTERMEDIARIES/PARTICIPANTS

Primary Dealers

Primary dealers (PDs) are important intermediaries in the government securities markets. They act as underwriters in the primary market, and as market makers in the secondary market. PDs underwrite a portion of the issue of government security that is floated for a pre-determined amount. The underwriting commitment of each PD is broadly decided on the basis of its size in terms of its net owned funds, its holding strength, the committed amount of bids and the volume of turnover in securities.

Brokers

Brokers play an important role in secondary debt market by bringing together counterparties and negotiating terms of the trade. It is through them that the trades are entered on the stock exchanges. The brokers are regulated by the stock exchanges and also by SEBI.

DEBT MARKET – REGULATORY FRAMEWORK

In India, a well developed banquet of laws such RBI Act, Law of Contract, Securities Contracts (Regulation) (SCRA) Act, Government Securities (GS) Act, Payment and Settlement Systems Act, Depositories Act, etc. define the legal framework for debt markets. The RBI Act has made it incumbent upon RBI to manage the public debt and also on Government to entrust public debt management to RBI. SCRA Act governs all the Contracts (transactions) in securities including Government Securities. The GS Act applied to Government Securities created and issued by the Central Government.

Role of RBI

The Reserve Bank of India manages the public debt and issues new loans on behalf of the Union and the State Governments under the powers derived from the Reserve Bank of India Act. It also undertakes cash and liquidity management for the Government of India and State Governments and administers the scheme of Ways and Means Advances (WMA).

Internal Debt Management Department of the RBI manages internal debt. This involves auctioning the Government debt from time to time, introduction of new instruments, smoothening the maturity structure of debt, placing of debt at market related rates and improving depth and liquidity of Government securities by developing active secondary market for them. The Government Securities Act, 2006 governs the Government Debt Market.

The Reserve Bank of India is, therefore, the main regulator for the Money Market. RBI is responsible for the market for repo/reverse repo transactions in Corporate debt. Issuance of Non-convertible Debentures Reserve Bank Directions, 2010 is also applicable for issuance of NCDs of original or initial maturity upto 1 year. Apart from its role as a regulator, it has to simultaneously fulfill several other important objectives viz. managing the borrowing program of the Government of India, controlling inflation, ensuring adequate credit at reasonable costs to various sectors of the economy, managing the foreign exchange reserves of the country and ensuring a stable currency environment.

RBI controls the interest rate policy. Earlier, it used to strictly control interest rates through a directed system of interest rates. Each type of lending activity was supposed to be carried out at a pre-specified interest rate. Over the years RBI has moved slowly towards a regime of market determined controls. RBI provides negotiated

dealing system which is an electronic platform for facilitating dealing in Government Securities and money market instruments.

Role of SEBI

The Securities and Exchange Board of India (SEBI) controls corporate debt market in cases where entities raise money from public through public issues.

It regulates the manner in which such money are raised and ensure a fair play for the retail investor. The issuers are required to make the retail investor aware, of the risks inherent in the investment, by way of disclosure. Being regulator for the Mutual Funds in India SEBI regulates the entry of new mutual funds in the industry and also the instruments in which mutual funds can invest.

Other Regulator

Apart from the two main regulators, the RBI and SEBI, there are several other regulators specific for different classes of investors. The Central Provident Fund Commissioner and the Ministry of Labour regulate the Provident Funds. Religious and Charitable trusts are regulated by some of the State governments of the states, in which these trusts are located.

SEBI (ISSUE OF CAPITAL AND DISCLOSURE REQUIREMENTS) REGULATIONS, 2009

Issue of debt securities that are convertible, either partially or fully or optionally into listed or unlisted equity shall be guided by the disclosure norms applicable to equity or other instruments offered on conversion in terms of SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009.

According to SEBI (ICDR) Regulations, 2009, convertible debt instruments means an instrument which creates or acknowledges indebtedness or 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.

Issue and listing of non-convertible debt securities, whether issued to the public or privately placed, are required to be made in accordance with the provisions of SEBI (Issue and Listing of Debt Securities) Regulations, 2008.

Credit Rating

An issuer can make an initial public offer of convertible debt instruments without making a prior public issue of its equity shares and listing thereof, subject to the following conditions:

- No company can make a public issue or rights issue of convertible debt instruments unless credit rating is obtained from one or more agencies i.e. credit rating is mandatory.
- The company is required to give the following details of credit ratings in case of a public issue or rights issue of convertible debt instruments:
 - (a) The names of all the credit rating agencies from which credit rating including unaccepted rating has been obtained for the issue of convertible debt instruments.
 - (b) All the credit ratings obtained during three years prior to the filing the offer document for any of the issuer's listed convertible debt instruments at the time of accessing the market through a convertible debt instrument.

Appointment of Debenture Trustee

The company is required to appoint one or more debenture trustees in accordance with the provisions of section 71 of the Companies Act, 2013 and SEBI (Debenture Trustees) Regulations, 1993.

The issuer is required to disclose the complete name and address of the debenture trustee in the annual report.

Debenture Redemption Reserve

The company is required to create a debenture redemption reserve in accordance with the provisions of section 71 of the Companies Act, 2013.

Redemption

The issuer is required to redeem the convertible debt instruments in terms of the offer document.

Documents to be Submitted Before Opening of the Issue

The lead merchant bankers shall submit a due diligence certificate from the debenture trustee in a prescribed form to SEBI along with the draft offer document.

Creation of Charge

If the issuer proposes to create a charge or security on its assets in respect of secured convertible debt instruments, it is required to ensure that-

- (i) such assets are sufficient to discharge the principal amount at all times;
- (ii) such assets are free from any encumbrance;
- (iii) 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 lessor for a second or *pari passu* charge has been obtained and submitted to the debenture trustee before the opening of the issue;
- (iv) the security/asset cover is required to 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.

Roll Over of Non Convertible Portion of Partly Convertible Debt Instruments

The non-convertible portion of partly convertible debt instruments issued by a listed issuer, the value of which exceeds fifty lakh rupees can be rolled over without change in the interest rate, subject to compliance with the provisions of Companies Act, 2013, and the following conditions—

- (a) 75% of the holders of the convertible debt instruments of the issuer have, through a resolution through postal ballot, approved the rollover.
- (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 SEBI 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.

However, the creation of fresh security and execution of fresh trust deed is not mandatory if the existing trust deed or the security documents provide for continuance of the security till redemption of secured convertible debt instruments.

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

Conversion of Optionally Convertible Debt Instruments into Equity Share Capital

(1) No issuer can 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 is not construed as consent for conversion of any convertible debt instruments.

(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 are required to be given the option of not converting the convertible portion into equity shares.

However, where the upper limit on the price of such instruments and justification thereon is determined and disclosed to the investors at the time of making the issue, it is not 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 Para (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 is required to 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.

However, this provision is not applicable if such redemption is in terms of the disclosures made in the offer document.

Restriction

An issuer can not 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.

However, 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.

Determination of Coupon Rate and Conversion Price

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

Minimum Promoter's Contribution

In case of public issue or composite issue of convertible debt securities

- the promoters shall contribute twenty per cent as stipulated for public issue under Regulation 32(1)



Either by way of equity shares or by way of subscription to the convertible securities.

In case of any issue of convertible securities which are convertible or exchangeable on different dates, then

- the promoters' 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.



by way of equity shares (conversion price being pre-determined)

In case of an initial public offer of convertible debt instruments without a prior public issue of equity shares, then

- the promoters are required to 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

Note:

- However, if the price of the equity shares allotted pursuant to conversion is not predetermined 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. **(In case of public issue or composite issue of convertible debt securities)**
- However, if the project is to be implemented in stages, the promoters' contribution is required to 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. **(In case of an initial public offer of convertible debt instruments)**

- (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 visited option, where any employer stock options are outstanding at the time of initial public offer.
- (ii) For computation of "weighted average price" :
 - Weight means the number of equity shares arising out of conversion of such specified securities into equity shares at various stages
 - price means the price of equity shares on conversion arrived at after taking into account pre-determined conversion price at various stages

Auditor's Certificate

The issuer is required to forward the details of utilisation of the funds raised through the convertible debt instruments duly certified by the statutory auditors of the issuer, to the debenture trustees at the end of each half-year.

Obligation of the Issuer

In case of an issue of convertible debt instruments, the issuer shall also give undertakings to the following effect in the offer document:

- (i) that the issuer shall forward the details of utilisation of the funds raised through the convertible debt instruments duly certified by the statutory auditors of the issuer, to the debenture trustees at the end of each half-year.
- (ii) that the issuer shall disclose the complete name and address of the debenture trustee in the annual report.
- (iii) that the issuer shall provide a compliance certificate to the convertible debt instrument holders (on yearly basis) in respect of compliance with the terms and conditions of issue of convertible debt instruments as contained in the offer document, duly certified by the debenture trustee.
- (iv) that the issuer shall furnish a confirmation certificate that the security created by the issuer in favour of the convertible debt instrument holders is properly maintained and is adequate to meet the payment obligations towards the convertible debt instrument holders in the event of default.
- (v) that necessary cooperation with the credit rating agency(ies) shall be extended in providing true and adequate information till the debt obligations in respect of the instrument are outstanding.

SEBI (ISSUE AND LISTING OF DEBT SECURITIES) REGULATIONS, 2008

SEBI issued (Issue and Listing of Debt Securities) Regulations, 2008 pertaining to issue and listing of debt securities which are not convertible, either in whole or part into equity instruments. They provide for a rationalized disclosure requirements and a reduction of certain onerous obligations attached to an issue of debt securities. These Regulations are applicable to –

- (i) public issue of debt securities and
- (ii) listing of debt securities issued through public issue or on private placement basis on a recognized stock exchange.

As per SEBI (ILDS) Regulations, 2008, debt securities means a non-convertible debt securities which create or acknowledge indebtedness, and include debenture, bonds and such offer securities of a body corporate or any statutory body constituted by virtue of a legislation, whether constituting a charge or the any sets of the body corporate or not, but excludes bonds issued by Government or such other bodies as may be specified by SEBI, securities receipts and securitized debt instruments.

ISSUE OF DEBT SECURITIES

Conditions

1. The issuer or the person in control of the issuer or its promoter or its director is restrained or prohibited or debarred by SEBI from accessing the securities market or dealing in securities; **or** the issuer or any of its promoters or directors is a wilful defaulter or it is in default of payment of interest or repayment of principal amount in respect of debt securities issued by it to the public, if any, for a period of more than six months.
2. It has made an application to one or more recognized stock exchanges for listing of such securities therein. If the application is made to more than one recognized stock exchanges, the issuer must choose one of them which has nationwide trading terminals as the designated stock exchange.
3. It has obtained in-principle approval for listing of its debt securities.
4. Credit rating including the unaccepted ratings obtained from more than one credit rating agencies, registered with SEBI shall be disclosed in the offer document.
5. The issuer can not issue debt securities for providing loan to or acquisition of shares of any person who is part of the same group or who is under the same management.

Appointment of Intermediaries

1. It shall enter into an arrangement with a depository registered with SEBI in accordance with the Depositories Act, 1996 and regulations made there under.
2. The issuer should appoint one or more merchant bankers registered with SEBI at least one of whom shall be a lead merchant banker.
3. The issuer is required to appoint one or more debenture trustees in accordance with the provisions of Section 71 of the Companies Act, 2013 and SEBI (Debenture Trustees) Regulations, 1993.

Disclosures of Material Information

1. The offer document must contain all material disclosures which are necessary for the subscribers of the debt securities to take an informed investment decision. The offer document contains the following:
 - (a) the disclosures specified in Section 26 of the Companies Act, 2013;

- (b) disclosure specified in Schedule I of these regulations;
 - (c) additional disclosures as may be specified by SEBI
2. The amount of minimum subscription which the issuer seeks to raise and underwriting arrangements shall be disclosed in the offer document.

Filing

The issuer shall file a draft offer document with the designated stock exchange through the lead merchant banker and also forward a copy of the draft & final offer document to SEBI.

Filing of Shelf Prospectus

(1) The following companies or entities may file shelf prospectus under section 31 of Companies Act, 2013 for public issuance of their debt securities,-

- (a) Public financial institutions as defined under clause (72) of section 2 of the Companies Act, 2013, and scheduled banks as defined under clause (e) of section 2 of the Reserve Bank of India Act, 1934; or
- (b) Issuers authorized by the notification of Central Board of Direct Taxes to make public issue of tax free secured bonds, with respect to such tax free bond issuances; or
- (c) Infrastructure Debt Funds – Non-Banking Financial Companies regulated by Reserve Bank of India; or
- (d) Non-Banking Financial Companies registered with Reserve Bank of India and Housing Finance Companies registered with National Housing Bank complying with the following criteria:
 - (i) having a net worth of at-least Rs.500 crore, as per the audited balance sheet of the preceding financial year;
 - (ii) having consistent track record of distributable profit for the last three years;
 - (iii) securities issued under the shelf prospectus have been assigned a rating of not less than “AA-” category or equivalent by a credit rating agency registered with SEBI;
 - (iv) no regulatory action is pending against the company or its promoters or directors before the SEBI, Reserve Bank of India or National Housing Bank;
 - (v) the issuer has not defaulted in the repayment of deposits or interest payable thereon, redemption of debentures or preference shares or payment of dividend to any shareholder, or repayment of any term loan or interest payable thereon to any public financial institution or banking company, in the last three financial years.

Or

- (e) Listed entities complying with the following criteria:
 - (i) whose public issued equity shares or debt securities are listed on recognized stock exchange for a period of at least three years immediately preceding the issue and have been complying with the listing agreement entered into between the issuer and the recognized stock exchanges where the said securities of the issuer are listed;
 - (ii) having a net worth of at-least Rs.500 crore, as per the audited balance sheet of the preceding financial year;
 - (iii) having consistent track record of distributable profit for the last three years;
 - (iv) securities issued under the shelf prospectus have been assigned a rating of not less than “AA-” category or equivalent by a credit rating agency registered with SEBI;

- (v) no regulatory action is pending against the company or its promoters or directors before the SEBI, Reserve Bank of India or National Housing Bank;
 - (vi) the issuer has not defaulted in the repayment of deposits or interest payable thereon, redemption of debentures or preference shares or payment of dividend to any shareholder, or repayment of any term loan or interest payable thereon to any public financial institution or banking company, in the last three financial years.
- (2) The issuer filing a shelf prospectus shall file a copy of an information memorandum with the recognised stock exchanges and SEBI, immediately on filing the same with the Registrar.
- (3) The information memorandum shall contain the disclosures specified in Companies Act, 1956 or Companies Act, 2013, whichever is applicable and rules made thereunder and shall include disclosures regarding summary term sheet, material updations including revision in ratings, if any along with the rating rationale and financial ratios specified in Schedule I, indicating the pre and post issue change.
- (4) Not more than four issuances shall be made through a single shelf prospectus.

Responsibilities of Merchant Banker

The lead merchant banker must ensure that –

- The draft offer document clearly specifies the names and contact particulars of the compliance officer of the lead merchant banker and the company including the postal and email address, telephone and fax numbers.
- All comments received on the draft offer document are suitably addressed and shall also furnish to SEBI a due diligence certificate as per these regulations prior to the filing of the offer document with the Registrar of Companies.
- The lead merchant banker shall, prior to filing of the offer document with the Registrar of Companies, furnish to SEBI a due diligence certificate as per schedule II of these regulations.

Mode of Disclosure

- The draft offer document shall be made public by posting it on the website of the designated stock exchange for seeking public comments for a period of seven working days from the date of filing the draft offer document with such exchange.
- The draft offer document can also be displayed on the website of the issuer, merchant bankers and the stock exchanges where the debt securities are proposed to be listed.
- The draft and final offer document shall be displayed on the websites of stock exchanges and shall be available for download in PDF / HTML formats.
- Where any person makes a request for a physical copy of the offer document, the same shall be provided to him by the issuer or lead merchant banker.

Prohibition of Mis-statements in the Offer Document

- The offer document shall not omit disclosure of any material fact which may make the statements made therein, in light of the circumstances under which they are made, misleading.
- The offer document or abridged prospectus or any advertisement issued by an issuer in connection with a public issue of debt securities shall not contain any false or misleading statement.

Advertisements

- The issuer should make an advertisement in a national daily with wide circulation, on or before the issue opening date and such advertisement, amongst other things must contain the disclosures specified in these regulations.
- An issuer should not issue an advertisement–
 - which is misleading in material particular or which contains any information in a distorted manner or which is manipulative or deceptive or extraneous matters.
 - which contain a statement, promise or forecast which is untrue or misleading and the advertisement shall be truthful, fair and clear.
 - during the subscription period any reference to the issue of debt securities or be used for solicitation.

On-line Issuances

An issuer proposing to issue debt securities to the public through the on-line system of the designated stock exchange shall comply with the relevant applicable requirements as may be specified by SEBI.

Issue Price

A company may determine the price of debt securities in consultation with the lead merchant banker and the issue may be at fixed price or the price may be determined through book building process in accordance with the procedure as may be specified by SEBI.

Minimum Subscription

The minimum subscription for public issue of debt securities shall be specified as 75% of the base issue size for both NBFCs and Non NBFC issuers. Further, if the issuer does not receive minimum subscription of its base issue size (75%), then the entire application monies shall be refunded within 12 days from the date of the closure of the issue. In the event, there is a delay, by the issuer in making the aforesaid refund, then the issuer shall refund the subscription amount along with interest at the rate of 15% per annum for the delayed period.

However, the issuers issuing tax-free bonds, as specified by CBDT, shall be exempted from the above proposed minimum subscription limit.

Explanation: In any public issue of debt securities, the base issue size shall be minimum Rs. 100 crores.

Optional Underwriting

A public issue of debt securities may be underwritten by an underwriter registered with SEBI and in such a case adequate disclosures regarding underwriting arrangement shall be disclosed in the offer document.

Trust Deed

A trust deed shall–

- (1) be executed by the issuer in favour of the debenture trustee within three months of the closure of the issue.
- (2) contain such clauses as may be prescribed under section 71 of the Companies Act, 2013 and those mentioned in Schedule IV of SEBI (Debenture Trustees) Regulations, 1993.
- (3) not contain a clause which has the effect of –

- limiting or extinguishing the obligations and liabilities of the debenture trustees or the issuer in relation to any rights or interests of the investors.
- limiting or restricting or waiving the provisions of the Act, these regulations and circulars or guidelines issued by SEBI.
- indemnifying the debenture trustees or the issuer for loss or damage caused by their act of negligence or commission or omission.

Debenture Redemption Reserve

- (1) The issuer shall create a debenture redemption reserve in accordance with the provisions of the Companies Act, 2013 and circulars issued by Central Government in this regard.
- (2) Where the company has defaulted in payment of interest on debt securities or redemption thereof or in creation of security as per the terms of the issue of debt securities, any distribution of dividend shall require approval of the debenture trustees.

Creation of Charge

- (1) The proposal to create a charge or security, if any, in respect of secured debt securities shall be disclosed in the offer document along with its implications.
- (2) An undertaking from the company is given in the offer document that the assets on which charge is created are free from any encumbrances and if the assets are already charged to secure a debt, the permissions or consent to create second or *pari pasu* charge on the assets of the issuer have been obtained from the earlier creditor.
- (3) The issue proceeds shall be kept in an escrow account until the documents for creation of security as stated in the offer document, are executed.

Right to recall or redeem prior to maturity

An issuer making public issue of debt securities may recall such securities prior to maturity date at his option (call) or provide such right of redemption prior to maturity date (put) to all the investors or only to retail investors, at their option, subject to the following:

- (a) Such right to recall or redeem debt securities prior to maturity date is exercised in accordance with the terms of issue and detailed disclosure in this regard is made in the offer document including date from which such right is exercisable, period of exercise (which shall not be less than three working days), redemption amount (including the premium or discount at which such redemption shall take place);
- (b) The issuer or investor may exercise such right with respect to all the debt securities issued or held by them respectively or with respect to a part of the securities so issued or held ;
- (c) In case of partial exercise of such right in accordance with the terms of the issue by the issuer , it shall be done on proportionate basis only;
- (d) No such right shall be exercisable before expiry of twenty four months from the date of issue of such debt securities;
- (e) Issuer shall send notice to all the eligible holders of such debt securities at least twenty one days before the date from which such right is exercisable;
- (f) Issuer shall also provide a copy of such notice to the stock exchange where the such debt securities are listed for wider dissemination and shall make an advertisement in the national daily having wide circulation indicating the details of such right and eligibility of the holders who are entitled to avail such right ;

- (g) Issuer shall pay the redemption proceeds to the investors along with the interest due to the investors within fifteen days from the last day within which such right can be exercised;
- (h) Issuer shall pay interest at the rate of fifteen per cent per annum for the period of delay, if any,
- (i) After the completion of the exercise of such right, the issuer shall submit a detailed report to the stock exchange for public dissemination regarding the debt securities redeemed during the exercise period and details of redemption thereof.

Redemption and Roll-over

- (1) The issuer shall redeem the debt securities in terms of the offer document.
- (2) An issuer desirous of rolling-over the debt securities issued by it, it shall do so only upon passing of a special resolution of holders of such securities and give twenty one days notice of the proposed roll over to them.
- (3) The notice shall contain disclosures with regard to credit rating and rationale for roll-over.
- (4) Prior to sending the notice to holders of debt securities, the issuer must file a copy of the notice and proposed resolution with the stock exchanges where such securities are listed, for dissemination of the same to public on its website.
- (5) The debt securities issued can be rolled over subject to the following conditions –
 - A special resolution has been passed by the holders of debt securities through postal ballot having the consent of not less than 75% of the holders by value of such debt securities.
 - At least one rating is obtained from a credit rating agency within a period of six months prior to the due date of redemption and is disclosed in the notice.
 - Fresh trust deed shall be executed at the time of such roll-over or the existing trust deed can be continued if the trust deed provides for such continuation.
 - Adequate security shall be created or maintained in respect of such debt securities to be rolled-over.
- (6) The issuer shall redeem the debt securities of all the debt securities holders, who have not given their positive consent to the roll-over.

Mandatory Listing

- (1) An issuer desirous of making an offer of debt securities to public shall make an application for listing to one or more recognized stock exchanges in terms of sub-section (1) of section 40 of the Companies Act, 2013.
- (2) It must comply with conditions of listing of such debt securities as specified in the Listing Agreement with the stock exchange where such debt securities are sought to be listed.
- (3) Where of the company has disclosed the intention to seek listing of debt securities issued on private placement basis, it shall forward the listing application along with the disclosures specified in Schedule I to the recognized stock exchange within fifteen days from the date of allotment of such debt securities.

SEBI has provided certain clarifications on aspects related to day count convention for debt securities issued under the SEBI (Issue and Listing of Debt Securities) Regulations, 2008.

- (a) If the interest payment date falls on a holiday, the payment may be made on the following working day however the dates of the future coupon payments would be as per the schedule originally stipulated at the time

of issuing the security. In other words, the subsequent coupon schedule would not be disturbed merely because the payment date in respect of one particular coupon payment has been postponed earlier because of it having fallen on a holiday.

For example:

Date of Issue of Corporate bonds: July 01, 2016

Date of Maturity: June 30, 2018

Date of coupon payments: January 01 and July 01

Coupon payable: semi-annually

In this case, January 01, 2017 is a Sunday, thus the coupon would be payable on January 02, 2017 i.e. the next working day. However the calculation for payment of interest will be only till December 31, 2016, which would have been the case if January 01, 2017 were not a holiday. Also, the next dates of payment would remain July 01, 2017 and January 01, 2018 despite the fact that one of the interest payment was made on January 02, 2017.

(b) In order to ensure consistency for interest calculation, a uniform methodology shall be followed for calculation of interest payments in the case of leap year, which shall be as follows:

In case of a leap year, if February 29 falls during the tenor of a security, then the number of days shall be reckoned as 366 days (Actual/Actual day count convention) for a whole one year period, irrespective of whether the interest is payable annually, half yearly, quarterly or monthly etc. It is thus emphasized that for a half yearly interest payment, 366 days would be reckoned twice as the denominator; for quarterly interest, four times and for monthly interest payment, twelve times.

(c) In order to ensure uniformity for payment of interest/redemption with respect to debt securities, interest/redemption payments shall be made only on the days when the money market is functioning in Mumbai.

CONDITIONS FOR PRIVATE PLACEMENT

1. An issuer may list its debt securities issued on private placement basis on a recognized stock exchange subject to the following conditions:
 - In compliance with the provisions of the Companies Act, 2013, rules prescribed there under and other applicable laws.
 - Credit rating has been obtained from at least one credit rating agency registered with SEBI.
 - Should be in dematerialized form.
 - The disclosures as provided in these regulation have been made.
 - Where application is made to more than one recognised stock exchange, the issuer shall choose one of them as the designated stock exchange
2. The issuer shall comply with conditions of listing of such debt securities as specified in the Listing Agreement with the stock exchange where such debt securities are sought to be listed.
3. The issuer making a private placement of debt securities and seeking listing thereof on a recognised stock exchange shall make disclosures in a disclosure document as specified in Schedule I of these regulations accompanied by the latest Annual Report of the issuer.
3. The designated stock exchange shall collect a regulatory fee from the issuer at the time of listing of debt securities issued on private placement basis.

As per section 42(1) of the Companies Act, 2013, a company may make an offer or invitation to subscribe to securities through issue of a private placement offer letter in Form PAS-4. The company shall maintain a complete

record of private placement offers in Form PAS-5 and a copy of such record along with the private placement offer letter in Form PAS-4 shall be filed with the Registrar with fee as provided in Companies (Registration Offices and Fees) Rules, 2014 and where the company is listed, with the SEBI within a period of thirty days of circulation of the private placement offer letter.

Filing of Shelf Disclosure Document

- An issuer making a private placement of debt securities and seeking listing thereof on a recognized stock exchange may file a Shelf Disclosure Document containing disclosures as provided in Schedule I of these regulations.
- The issuer is not required to file disclosure document, while making subsequent private placement of debt securities for a period of 180 days from the date of filing of the shelf disclosure document.
- However, while making any private placement under Shelf Disclosure Document, it shall file with the concerned stock exchange updated disclosure document with respect to each tranche, containing details of the private placement and material changes, if any, in the information provided in Shelf Disclosure Document.

Consolidation and re-issuance

An issuer may carry out consolidation and re-issuance of its debt securities in the manner as may be specified by SEBI from time to time, subject to the fulfillment of the following conditions:

- a) the articles of association of the issuer shall not have any provision, whether express or implied, contrary to such consolidation and re-issuance;
- b) the issue is through private placement;
- c) the issuer has obtained fresh credit rating for each re-issuance from at least one credit rating agency registered with SEBI and is disclosed;
- d) such ratings shall be revalidated on a periodic basis and the change, if any, shall be disclosed;
- e) appropriate disclosures are made with regard to consolidation and re-issuance in the Term Sheet.

International Securities Identification Number

Any issuer issuing debt securities on private placement basis, shall comply with the conditions relating to the issue of International Securities Identification Number, as may be specified by SEBI from time to time.

RELAXATION OF STRICT ENFORCEMENT OF RULE 19 OF SECURITIES CONTRACTS (REGULATION) RULES, 1957

In exercise of the powers conferred by sub-rule (7) of rule 19 of the Securities Contracts (Regulation) Rules, 1957, SEBI relaxed the strict enforcement of:

- (1) Sub-rules (1) and (3) of rule 19 of the said rules in relation to listing of debt securities issued by way of a public issue or a private placement.
- (2) Clause (b) of sub-rule (2) of rule 19 of the said Rules in relation to listing of debt securities–
 - (i) Issued by way of a private placement by any company.
 - (ii) Issued to public by an infrastructure company, a Government Company, a statutory authority or corporation or any special purpose vehicle set up by any of them, which is engaged in infrastructure sector.

LISTING AND TRADING OF DEBT SECURITIES

Continuous Listing

- (1) All the issuer shall comply with the conditions of listing specified in the respective listing agreement for debt securities while making public issues of debt securities or seeking listing of debt securities issued on private placement basis.
- (2) Each rating obtained by the issuer shall be periodically reviewed by the registered credit rating agency and any revision in the rating shall be promptly disclosed by the issuer to the stock exchange(s) where the debt securities are listed.
- (3) Any change in rating shall be promptly disseminated to investors and prospective investors in such manner as the stock exchange may determine from time to time.
- (4) Debenture trustee must disclose the information to the investors and the general public by issuing a press release in any of the following events:
 - (a) default by the issuer to pay interest on debt securities or redemption amount;
 - (b) failure to create a charge on the assets;
 - (c) revision of rating assigned to the debt securities.

Trading

- (1) While issuing debt securities to the public or on a private placement basis, which are listed in recognized stock exchanges, shall be traded and such trades shall be cleared and settled in recognized stock exchanges it should satisfy the conditions as specified by SEBI.
- (2) The trades of debt securities which have been made over the counter shall be reported on a recognized stock exchange having a nationwide trading terminal or such other platform as may be specified by SEBI.
- (3) SEBI may specify conditions for reporting of trades on the recognized stock exchange or other platform

Information to be Displayed on Website

- The disclosures as specified in Schedule-I accompanied by the latest annual report shall be made on the websites of stock exchanges where such securities are proposed to be listed and shall be available for download in PDF / HTML formats.
- The issuer, the respective debenture trustees and stock exchanges shall disseminate all information and reports including compliance reports filed by the issuers and the debenture trustees regarding the debt securities to the investors and the general public by placing them on their websites.
- The information shall also be placed on the websites, if any, of the debenture trustee, the issuer and the stock exchanges.

Obligations of Debenture Trustee

- (1) The debenture trustee shall prior to the opening of the public issue, furnish to SEBI a due diligence certificate as per of these regulations.
- (2) The debenture trustee shall be vested with the requisite powers for protecting the interest of holders of debt securities including a right to appoint a nominee director on the Board of the issuer in consultation with institutional holders of such securities.

- (3) The debenture trustee shall carry out its duties and perform its functions under these regulations, the SEBI (Debenture Trustees) Regulations, 1993, the trust deed and offer document, with due care, diligence and loyalty.
- (4) The debenture trustee shall ensure disclosure of all material events on an ongoing basis.
- (5) The debenture trustees shall supervise the implementation of the conditions regarding creation of security for the debt securities and debenture redemption reserve.

Obligations of the Issuer, Lead Merchant Banker, etc.

- (1) The issuer shall ensure that all the material facts disclosed in the offer documents issued or distributed to the public are true, fair and adequate and there is no mis-leading or untrue statements or mis-statement in the offer document.
- (2) The Merchant Banker shall ensure verify and confirm that the disclosures made in the offer documents are true, fair and adequate and the issuer is in compliance with these regulations as well as all transaction specific disclosures specified in section 26 of the Companies Act, 2013.
- (3) The issuer shall treat the applicant in a fair and equitable manner as per the procedures as may be specified by SEBI.
- (4) In respect of assignments undertaken for issue, offer and distribution of securities to the public the intermediaries shall be responsible for the due diligence.
- (5) A person shall not employ any device, scheme or artifice to defraud in connection with issue or subscription or distribution of debt securities which are listed or proposed to be listed on a recognized stock exchange.
- (6) The issuer and the merchant banker shall ensure that the security created to secure the debt securities is adequate to ensure 100% asset cover for the debt securities.

Disclosure chart		
Equity already listed	Type of offering	Manner of disclosures
Yes	Public offering	<ul style="list-style-type: none"> – Material disclosures from section 26 of Companies Act, 2013 – Sch I of the Regulations – Simplified debt listing agreement.
Yes	Private placement with listing	<ul style="list-style-type: none"> – Sch I of the Regulations – Simplified debt listing agreement – (reference to) last annual report
No	Public offering	<ul style="list-style-type: none"> – Material disclosures from section 26 of Companies Act, 2013 – Sch I of the Regulations – Debt listing agreement
No	Private placement with listing	<ul style="list-style-type: none"> – Sch I of the Regulations – Debt listing agreement – (reference to) last annual report

Electronic book mechanism for issuance of debt securities on private placement basis

SEBI (Issue and Listing of Debt Securities) Regulations, 2008, govern public issue of debt securities and listing of debt securities issued through public issue or on private placement basis, on a recognized stock exchange. Regulation 31(2) of SEBI (ILDS) Regulations, 2008 *inter alia* provides that :

“In particular, and without prejudice to the generality of the foregoing power and provisions of these regulations, such orders or circulars may provide for all or any of the following matters, namely: (a) Electronic issuances and (b) other issue procedures including the procedure for price discovery; “

In order to streamline procedures for issuance of debt securities on private placement basis and enhance transparency to discover prices, SEBI has laid down a framework for issuance of debt securities on private placement basis through an electronic book mechanism.

Electronic book mechanism would be mandatory for all private placements of debt securities in primary market with an issue size of Rs.500 crores and above, inclusive of green shoe option, if any.

Eligible Issuer

The following issuers shall have an option to follow either electronic book mechanism or the existing mechanism:

- issues with a single investor and where coupon rate are fixed. However arrangers acting as underwriters shall not be considered as single investors.
- issues wherein the issue size is less than Rs. 500 crores, inclusive of green shoe option, if any.

However, for all issues below Rs.500 crore, issuer shall disclose the coupon, yield, amount raised, number of investors and category of investors to the Electronic Book Provider and/ or to the information repository for corporate debt market as notified by SEBI.

Electronic book provider (EBP)

The electronic book mechanism shall be provided by recognized stock exchange(s) only after obtaining prior approval from SEBI.

The following are eligibility conditions for a recognised stock exchange to act as EBP:-

- EBP shall provide an on-line platform for receiving bids in private placement of debt securities.
- EBP shall own website/ URL (hereinafter referred to as bidding portal) on which it proposes to offer its services.
- EBP shall have all the necessary infrastructure like adequate office space, equipment's, risk management capabilities, manpower and other information technology infrastructure to effectively discharge the activities of EBP.
- EBP shall ensure that there is adequate backup, disaster management and recovery plans for the electronic book mechanism so provided by EBP.
- The EBP shall ensure safety, secrecy, integrity and retrievability of data.
- The electronic book mechanism so provided by EBP would be subject to periodic audit by Certified Information Systems Auditor (CISA) under Annual System Audit prescribed by SEBI.

Participants in Electronic book mechanism

- Arranger, if any, appointed by the issuer, merchant bankers, RBI registered primary dealers or any other registered intermediaries, may act as the arranger. Arranger shall be categorised as a Category 1 Participant who may enter bids on EBP either on proprietary basis or for other participants such as High Net worth Individuals (HNIs), Institutional investors etc.

- Sub-arranger appointed by the arranger, any broker registered with SEBI may act as a sub-arranger. Sub-arranger shall be categorised as a Category 1 Participant who may enter bids on EBP either on proprietary basis or for other participants such as High Net worth Individuals (HNIs), Institutional investors etc.
- Institutional investors shall be categorised as Category 2 Participants who may enter bids on proprietary basis or may participate through an arranger/sub-arranger.

Procedure for electronic book mechanism

The procedure to be followed for electronic book mechanism is as follows:

Pre-Bid Procedure

- Participants shall be required to enroll with EBP before entering bids and only eligible participants may participate in the bidding process.
- Qualified Institutional Buyer and other eligible bidders (as determined by the issuer) may participate in the bidding process.

However, in case the issuer is NBFC which are registered with RBI and HFCs registered with National Housing Bank, QIBs, eligible bidders and other participants enrolled with EBP, may participate in the bidding process subject to the RBI requirements, if any prescribed in this regard.

- The EBP shall provide the details of QIBs and other participants enrolled with EBP (if applicable) to the issuer.
- All enrolled participants (other than QIBs) who wish to participate on any issue either directly or through arranger, as applicable would be required to pre-register before being allowed to access to the PPM or other information with respect to issue.

However, if the number of such pre-registration of participants exceeds 200 in a year, then the eligible bidders would be determined by draw of lots or first come first served basis undertaken by the EBP in consultation with issuer so as to limit participants to 200 in a year.

- The bidding time window (bidding time, cooling period, renegotiation window etc.) shall be decided by issuer in consultation with the EBP which shall be disclosed to the bidders by EBP in advance.

Bidding Procedure

- Bidding shall be allowed in the bidding time window specified by the issuer.
- Bid shall be made by way of entering bid amount in Rupees (INR) and coupon/yield in basis points (bps).
- Participants shall be allowed to enter multiple bids i.e. single participant may enter more than one bid.
- EBP shall provide a facility for generation of acknowledgement number against such bids.

Post Bidding Procedure

- All bids received within bidding time window shall be provided by EBP to the issuer after bidding process is over.
- Issuer shall have the option to accept or reject bids received, if the issuer agrees to the yield so discovered.
- Issuer shall provide details of accepted bids to depositories to make allotment.
- EBP shall display bid details on the end of the bidding time window.
- At the end of the bidding time window, EBP shall on an anonymous basis, disclose the aggregate

volume data, including yield, amount including the amount of oversubscription, total bids received, rating(s), category of investor etc., to avoid any speculations.

- For issues below Rs.500 crore, issuer shall upload details as mentioned above with EBP and/or with information repository for corporate debt market as notified by SEBI, in the format as specified.
- EBP shall upload the allotment data on its website to be made available to the public.

GREEN DEBT SECURITIES

SEBI (Issue and Listing of Debt Securities) Regulations, 2008 (“SEBI ILDS Regulations”), governs public issue of debt securities and listing of debt securities issued through public issue or on private placement basis, on a recognized stock exchange. For public issue and listing of Green Debt Securities and listing of privately placed Green Debt Securities, in addition to the requirements as prescribed under SEBI ILDS Regulations and Circulars made thereunder, following shall also be applicable.

Meaning of Green Debt Securities

A Debt Security shall be considered as “**Green or Green Debt Securities**”, if the funds raised through issuance of the debt securities are to be utilised for project(s) and/or asset(s) falling under any of the following broad categories:

- a) Renewable and sustainable energy including wind, solar, bioenergy, other sources of energy which use clean technology etc.;
- b) Clean transportation including mass/public transportation etc.;
- c) Sustainable water management including clean and/or drinking water, water recycling etc.;
- d) Climate change adaptation;
- e) Energy efficiency including efficient and green buildings etc.;
- f) Sustainable waste management including recycling, waste to energy, efficient disposal of wastage etc.;
- g) Sustainable land use including sustainable forestry and agriculture, afforestation etc.;
- h) Biodiversity conservation;
- i) Any other category as may be specified by SEBI, from time to time.

Disclosures in Offer Document/Disclosure Document and other requirements

The issuer of a Green Debt Securities shall make following disclosures:

- a) A statement on environmental objectives of the issue of Green Debt Securities;
- b) Brief details of decision-making process issuer has followed/would follow for determining the eligibility of project(s) and/or asset(s), for which the proceeds are been raised through issuance of Green Debt Securities. An indicative guideline of the details to be provided is as under:
 - process followed/to be followed for determining how the project(s) and/or asset(s) fit within the eligible green projects categories;
 - the criteria, making the project(s) and/or asset(s) eligible for using the Green Debt Securities proceeds; and
 - environmental sustainability objectives of the proposed green investment.
- c) Issuer shall provide the details of the system/procedures to be employed for tracking the deployment of the proceeds of the issue.

- d) Details of the project(s) and/or asset(s) or areas where the issuer, proposes to utilise the proceeds of the issue of Green Debt Securities, including towards refinancing of existing green project(s) and/or asset(s), if any.
- e) The issuer may appoint an independent third party reviewer/certifier, for reviewing /certifying the processes including project evaluation and selection criteria, project categories eligible for financing by Green Debt Securities, etc. Such appointment is optional and shall be disclosed in the offer document.

Continuous Disclosure

An issuer who has listed its Green Debt Securities, alongwith compliances as under SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, shall provide following disclosures along with its annual report and financial results:

- a) Details of utilisation of the proceeds and unutilized proceeds of the issue, as disclosed in offer document/ disclosure document. These details shall be provide along with the half yearly and annual financial results.

However, the utilisation of the proceeds shall be verified by the report of an external auditor, to verify the internal tracking method and the allocation of funds towards the project(s) and/or asset(s), from the proceeds of Green Debt Securities.

- b) Other additional disclosures have to be provided along with annual report:

- List of project(s) and/or asset(s) to which proceeds of the Green Debt Securities have been allocated/ invested including a brief description of such project(s) and/or asset(s) and the amounts disbursed.

However, where confidentiality agreements limit the amount of details that can be made available about specific project(s) and/or asset(s), information shall be presented about the areas in which such project(s) and/or asset(s) fall into.

- Qualitative performance indicators and, where feasible, quantitative performance measures of the environmental impact of the project(s) and/or asset(s). If the quantitative benefits/impact cannot be ascertained, then the said fact may be appropriately disclosed along with the reasons for non-ascertainment of the benefits/impact on the environment.
- Methods and the key underlying assumptions used in preparation of the performance indicators and metrics;

Obligations of the issuer

An issuer of Green Debt Securities shall :

- Maintain a decision-making process which it uses to determine the continuing eligibility of the project(s) and/or asset(s). This includes, without limitation a statement on the environmental objectives of the Green Debt Securities and a process to determine whether the project(s) and/or asset(s) meet the eligibility requirements.
- Ensure that all project(s) and/or asset(s) funded by the proceeds of Green Debt Securities, meet the documented objectives of Green Debt Securities.
- Utilise the proceeds only for the stated purpose, as disclosed in the offer document.

An issuer of Green Debt Securities or any agent appointed by the issuer, if follows any globally accepted standard(s) for the issuance of Green Debt Securities including measurement of the environmental impact, identification of the project(s) and/or asset(s), utilisation of proceeds, etc., shall disclose the same in the offer document/disclosure document and/or in continuous disclosures.

SECURITISED DEBT INSTRUMENT

The Securities Contracts (Regulation) Act, 1956 was amended in 2007 to include under the definition of securities any certificate or instrument (by whatever name it is called) issued to an investor by any issuer who is a special purpose distinct entity possessing any debt or receivable, including mortgage debt assigned to such entity, and acknowledging the beneficial interest of the investor in such debt or receivable, including mortgage debt, as the case maybe.

Securitization involves the pooling of financial assets and the issuance of securities that are re-paid from the cash flows generated by these assets. Common assets for securitization include credit cards, mortgages, auto and consumer loans, student loans, corporate debt, export receivable, and offshore remittances.

Securitized debt instruments are regulated by the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002, SEBI (Public Offer and Listing of Securitized Debt Instruments) Regulations, 2008 for listing on stock exchanges and the Securitization Companies and Reconstruction Companies (Reserve Bank) Guidelines and Directions, 2003.

Here, we will discuss SEBI (Public offer and Listing of Securitized Debt Instruments) Regulations, 2008 which is as under:

SEBI (PUBLIC OFFER AND LISTING OF SECURITISED DEBT INSTRUMENTS) REGULATIONS, 2008

SEBI notified SEBI (Public Offer and Listing of Securitized Debt Instruments) Regulations, 2008 on May 26, 2008 taking into account the market needs, cost of the transactions, competition policy, the professional expertise of credit rating agencies, disclosures and obligations of the parties involved in the transaction and the interest of investors in such instruments.

Eligibility Criteria

- A person can not make a public offer of securitized debt instruments or seek listing for such securitized debt instruments unless –
 - (a) it is constituted as a special purpose distinct entity;
 - (b) all its trustees are registered with the SEBI under the SEBI (Public Offer and Listing of Securitized Debt Instruments) Regulations, 2008; and
 - (c) it complies with all the applicable provisions of these regulations and the Act.
- The requirement of obtaining registration is not applicable for the following persons, who may act as trustees of special purpose distinct entities:
 - (a) any person registered as a debenture trustee with SEBI;
 - (b) any person registered as a securitization company or a reconstruction company with the RBI under the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002;
 - (c) the National Housing Bank established by the National Housing Bank Act, 1987;
 - (d) the National Bank for Agriculture and Rural Development established by the National Bank for Agriculture and Rural Development Act, 1981.
 - (e) any scheduled commercial bank other than a regional rural bank;
 - (f) any public financial Institution as defined under clause (72) of section 2 of the Companies Act, 2013; and
 - (g) any other person as may be specified by SEBI.

However, these persons and special purpose distinct entities of which they are trustees are required to comply with all the other provisions of the SEBI (Public Offer and Listing of Securitized Debt Instruments)

Regulations, 2008. However, these Regulations are not applicable for the National Housing Bank and the National Bank for Agriculture and Rural Development, to the extent of inconsistency with the provisions of their respective Acts.

- An applicant seeking registration to act as a trustee shall,-
 - (a) have a networth of not less than two crore rupees.
 - (b) have in its employment a minimum of two persons who, between them, have atleast five years experience in activities related to securitisation and atleast one among them shall have a professional qualification in law from any university or institution recognised by the Central Government or any State Government or a foreign university.

However, the above-said requirements are not applicable on the National Housing Bank established by the National Housing Bank Act, 1987 and National Bank for Agriculture and Rural Development established by the National Bank for Agriculture and Rural Development Act, 1981.

Launching of schemes

- (1) A special purpose distinct entity may raise funds by making an offer of securitized debt instruments by formulating schemes in accordance with the SEBI (Public Offer and Listing of Securitized Debt Instruments) Regulations, 2008.
- (2) Where there are multiple schemes, the special purpose distinct entity is required to maintain separate and distinct accounts for each such scheme, and should not combine the asset pools or the realizations of a scheme with those of other schemes.
- (3) A special purpose distinct entity and the trustees should ensure that the realizations of debts and receivables are held and correctly applied towards the redemption of securitized debt instruments issued under the respective schemes, or towards the payment of the returns on such instruments, or towards other permissible expenditures of the scheme.
- (4) The terms of issue of the securitized debt instruments may provide for the exercise of a clean-up call option by the special purpose distinct entity, subject to adequate disclosures.
- (5) No expenses should be charged to the scheme in excess of the allowable expenses as may be specified in the scheme, and any such expenditure, if incurred, should be borne by the trustees.

Winding up of schemes

A scheme may be wound up in the event of the following:

- when the securitised debt instruments have been fully redeemed as per the scheme;
- upon legal maturity as stated in the terms of issue of the securitised debt instrument. However, if any debt or receivable is outstanding on legal maturity, the trustees shall dispose off the same in accordance with the scheme and distribute the proceeds;
- by vote of investors by a special resolution.

Offer to the public

- Any reference in these regulations to offering securitised debt instruments to the public shall be construed as including a reference to offering them to any section of the public.
- No offer shall be treated as made to the public, if the offer can properly be regarded, in all the circumstances –
 - (a) as not being likely to result, directly or indirectly, in the securitised debt instruments becoming available for subscription or purchase by persons other than those receiving the offer;

(b) otherwise as being the domestic concern of the persons making and receiving the offer.

However, above mentioned conditions apply only in respect of securitised debt instruments which belong to the same tranche and which are pari passu in all respects.

- Any offer of securitised debt instruments made to fifty or more persons in a financial year shall always be deemed to have been made to the public.

Submission of draft offer document and filing of final offer document.

- No special purpose distinct entity or trustee thereof shall make an offer of securitised debt instruments to the public unless it files a draft offer document with SEBI at least fifteen working days before the proposed opening of the issue.
- Such offer document shall be filed along with the minimum filing fee as mentioned in Schedule II of these regulations.
- However, the balance filing fee provided in Schedule II shall be paid to SEBI within seven days of closure of the public offer.
- If SEBI specifies any changes to be made in the offer document within the said period of fifteen working days, the special purpose distinct entity and trustee thereof shall carry out such changes in the draft offer document prior to filing it with the designated stock exchange or issuing it.
- The final offer document shall be filed with SEBI and with every recognised stock exchange to which an application for listing of the securitised debt instruments is proposed to be made prior to its issuance to public.

Arrangements for dematerialisation

- Prior to submitting the draft offer document with SEBI, the special purpose distinct entity shall enter into an arrangement with a registered depository for dematerialisation of the securitised debt instruments that are proposed to be issued to the public.
- The special purpose distinct entity shall give an option to the investors to receive the securitised debt instruments either in the physical form or in dematerialised form.
- The holders of dematerialised instruments shall have the same rights and liabilities as holders of physical instruments.

Offer period

A public offer of securitised debt instruments shall not remain open for more than thirty days.

Minimum subscription

The offer document shall disclose the minimum subscription it seeks to raise under the scheme.

No securitised debt instruments shall be allotted under the public offer unless subscriptions have been received in respect of the minimum number of securitised debt instruments which will constitute minimum subscription.

Here “minimum subscription” refers to the amount which, in the opinion of the directors of the originator and trustees of the special purpose distinct entity, must be raised by issue of securitised debt instruments.

In the event of non-receipt of minimum subscription or refusal of listing by any recognised stock exchange, all application moneys received in the public offer shall be refunded forthwith to the applicants.

Allotment and other obligations

- The securitised debt instruments shall be allotted to the investors within the following time periods:-

- (a) in case of dematerialized securitised debt instruments – within five days of closure of the offer;
- (b) in case of securitised debt instruments in the physical form – the certificates shall be dispatched within eight days of closure of the offer.
- No special purpose distinct entity shall retain any oversubscription received in any public offer.
- In the event of over-subscription, the allotment shall be made as per the basis of allotment finalized in consultation with the recognized stock exchanges to which an application for listing was made.
- The special purpose distinct entity shall dispatch refund orders to unsuccessful or partially successful applicants within eight days of closure of the offer.
- In a case where the issue proceeds become liable to be refunded in accordance with the disclosures made in the offer document, the special purpose distinct entity shall dispatch refund orders to the applicants within eight days of closure of the offer.
- Where the allotment is not made within the time period mentioned or where the certificates are not dispatched within the time, the special purpose distinct entity and every trustee thereof, and where any such trustee is a body corporate, every director thereof, who is in default shall, on and from the expiry of such period, be jointly and severally liable to pay interest at the rate of fifteen per cent per annum to the concerned applicants.
- Where the refund orders are not dispatched within the time mentioned, the special purpose distinct entity and every trustee thereof, and where any such trustee is a body corporate, every director thereof, who is in default shall, on and from the expiry of the eighth day, be jointly and severally liable to repay that money with interest at the rate of fifteen per cent per annum.
- Above sub-regulations shall have effect without prejudice to any other provisions of these regulations or any other law.
- Credit to demat accounts of the allottees shall be made by the issuer within two working days from the date of allotment.

Rights of investors in securities issued by special purpose distinct entity

- The trust deed or other instrument comprising the terms of issue of the securitised debt instruments issued by a special purpose distinct entity shall provide that investors holding such securitised debt instruments have such beneficial interest in the underlying debt or receivables as may have been conferred by the scheme.
- In the event of failure of the special purpose distinct entity to redeem any securitised debt instruments offered through an offer document or listed, within the time and in accordance with the conditions stated in the offer document or other terms of issue, the investors holding not less than ten per cent in nominal value of such securitised debt instruments shall be entitled to call a meeting of all such investors.
- In such meeting, the investors may move a motion to–
 - (a) call upon the trustee and the special purpose distinct entity to wind up the scheme and distribute the realisations;
 - (b) remove the trustee;
 - (c) appoint a new trustee in place of the one removed under clause (b):

However, any such decision shall be taken by means of a special resolution of the investors of the scheme and sections 109 and 114 of the Companies Act, 2013 shall mutatis mutandis apply to such special resolution. However, the new trustee appointed is registered with SEBI under these regulations or is exempted from such registration.

- The trustee and the special purpose distinct entity shall take all reasonable steps to carry out the resolutions passed by the investors.

- Any reasonable expenses incurred in calling and holding a meeting and any reasonable expenses incurred by the trustee or the new trustee, as the case may be, in winding up the scheme and incidental activities shall be met from or reimbursed out of realisations from the asset pool.
- The terms of issue of securitised debt instruments shall not be adversely varied without the consent of the investors.
- The investors shall be deemed to have given their consent to variation if and only if twenty one days notice is given to them of the proposed variation and it is approved by a special resolution passed by them through postal ballot.
- Sections 114 and 117 of the Companies Act, 2013 and the rules framed thereunder shall mutatis mutandis apply to the special resolution referred above.

Listing Agreement

Every special purpose distinct entity desirous of listing securitised debt instruments on a recognised stock exchange, shall execute an agreement with such stock exchange.

Every special purpose distinct entity which has previously entered into agreements with a recognised stock exchange to list securitised debt instruments shall execute a fresh listing agreement with such stock exchange within six months of the date of notification of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015.

Transferability of securitised debt instruments

The securitised debt instruments issued to the public or listed on a recognized stock exchange in accordance with these regulations shall be freely transferable.

Rights of investors in securities issued by special purpose distinct entity

The trust deed or other instrument comprising the terms of issue of the securitised debt instruments issued by a special purpose distinct entity shall provide that investors holding such securitised debt instruments have such beneficial interest in the underlying debt or receivables as may have been conferred by the scheme.

In the event of failure of the special purpose distinct entity to redeem any securitised debt instruments offered through an offer document or listed, within the time and in accordance with the conditions stated in the offer document or other terms of issue, the investors holding not less than ten per cent in nominal value of such securitised debt instruments shall be entitled to call a meeting of all such investors.

Mandatory Listing

A special purpose distinct entity desirous of making an offer of securitized debt instruments to the public shall make an application for listing to one or more recognized stock exchanges in terms of Sub-section (2) of Section 17A of the Securities Contracts (Regulation) Act, 1956.

Minimum public offering for listing

For the public offers of securitized debt instruments, the special purpose distinct entity or trustee should satisfy the recognized stock exchange(s) (to which a listing application is made) that each scheme of securitized debt instruments was offered to the public for subscription through advertisements in newspapers for a period of not less than two days, and that the applications received in pursuance of the offer were allotted in accordance with these regulations and the disclosures made in the offer document.

In the case of a private placement of securitized debt instruments, the special purpose distinct entity shall file listing particulars with the recognized stock exchange, along with the listing application, containing such information as may be necessary for any investor in the secondary market to make an informed investment decision in respect of its securitized debt instruments and the special purpose distinct entity shall promptly disseminate such information, as prescribed, in such manner as the recognized stock exchange(s) may determine from time to time.

All the credit ratings obtained, including the unaccepted ratings, if any, should be disclosed in the listing particulars filed with the recognized stock exchange(s).

Continuous listing conditions

The special purpose distinct entity or trustee thereof shall submit such information, including financial information relating to the schemes to the stock exchange and investors and comply with such other continuing obligations as may be stipulated in the listing agreement.

Trading of securitized debt instruments

The securitized debt instruments issued to the public or on a private placement basis that are listed in recognized stock exchanges shall be traded, and such trades shall be cleared and settled in the recognized stock exchanges, subject to the conditions specified by SEBI.

MUNICIPAL BONDS

The Bangalore Municipal Corporation was the first municipal civil corporation in the country to issue a municipal bonds with a state guarantee in 1997. The debt market in India for municipal securities has grown considerably since the issuance of Municipal bonds in the country without State Government Guarantee by Ahmedabad Municipal Corporation in 1998 for financing infrastructure projects in the city. Since 1998, other cities that have accessed the capital markets through municipal bonds without state government guarantee include Nashik, Nagpur, Ludhiana, and Madurai. In most cases, bond proceeds have been used to fund water and sewerage schemes or road projects. The last issuance was done by Greater Vishakhapatnam Municipal Corporation for Rs 30 Crores in 2010.

The Government of India, in order to boost the municipal bond market, allowed the municipalities to issue tax-free municipal bonds. The central government amended the Income Tax Act (1961 vide the Finance Act 2000), whereby interest income from bonds issued by local authorities was exempted from income tax. The GOI issued guidelines for issue of tax-free municipal bonds in February 2001. These guidelines stipulate eligible issuers, use of funds, essential pre-conditions, maturing period, buy-back, nature of issue and tax benefits, ceiling amount for a project, compulsory credit rating, and external monitoring of the tax-free municipal bond.

Taking into consideration the above, SEBI placed on its website a concept paper, proposing a framework, governing issuance and listing of debt securities by the Municipalities, along with the draft SEBI (Issue and Listing of Debt Securities by Municipality) Regulations, 2015 for seeking public comments on the same.

After receiving representations and suggestions SEBI approved the draft Regulations on its Board Meeting dated 22 March, 2015 and notified the SEBI (Issue and Listing of Debt Securities by Municipality) Regulations, 2015 on July 15, 2015. These regulations discuss the eligibility requirement for public issue, listing of debt securities requirement for both public issues and private placement, conditions for continuous and trading of debt securities, obligations of intermediaries and issuer provisions. These regulations are in line with the Government of India guidelines for issue of tax-free bonds by Municipalities.

SEBI (ISSUE AND LISTING OF DEBT SECURITIES BY MUNICIPALITIES) REGULATIONS, 2015

These regulations shall apply to –

- (a) public issue of debt securities; and
- (b) listing of debt securities issued through public issue or on private placement basis on a recognised stock exchange

Here, “general obligation bonds” means debt securities where principal and interest are serviced through tax proceeds of the municipality.

“Revenue bonds” means debt securities which are serviced by revenues from one or more projects.

“Municipality” means an institution of self-government constituted under Article 243Q of the Constitution of India.

General conditions

An issuer making public issue of debt securities shall only issue revenue bonds.

No issuer shall make a public issue of revenue bonds unless following conditions are complied with:

- (a) it has made an application to one or more recognised stock exchanges for listing of such securities therein. However, where the application is made to more than one recognised stock exchanges, the issuer shall choose one of them as the designated stock exchange. Further, where any of such stock exchanges have nationwide trading terminals, the issuer shall choose one of them as the designated stock exchange;

Explanation.—For any subsequent public issue, the issuer may choose a different stock exchange as a designated stock exchange subject to the requirements of this regulation;

- (b) it has obtained in-principle approval for listing of its revenue bonds on the recognised stock exchanges where the application for listing has been made;
- (c) municipality shall have surplus income as per its Income and Expenditure Statement, in any of the immediately preceding three financial years or any other financial criteria as may be specified by SEBI from time to time. However, a corporate municipal entity shall not have negative net worth in any of immediately preceding three financial years.
- (d) municipality shall not have defaulted in repayment of debt securities or loans obtained from banks or financial institutions, during the last three hundred and sixty five days. However, where the issuer is a corporate municipal entity, the requirements at clauses (b) and (d) shall be complied by the municipality which is being financed.

Advertisements for public issues

- The issuer may make an advertisement in a national daily with wide circulation, on or before the issue opening date and such advertisement shall, amongst other things, contain the disclosures as per Schedule IV of these regulations.
- No issuer shall issue an advertisement which is misleading in material particular or which contain any information in a distorted manner or which is manipulative or deceptive.
- The advertisement shall be truthful, fair and clear and shall not contain a statement, promise or forecast which is untrue or misleading.
- Any advertisement issued by the issuer shall not contain any matters which are extraneous to the contents of the offer document.
- The advertisement shall urge the investors to invest only on the basis of information contained in the offer document.
- Any promotional or educative advertisement issued by the issuer during the subscription period shall not make any reference to the issue of revenue bonds or be used for solicitation.

Minimum subscription

- The issuer may decide the amount of minimum subscription which it seeks to raise by issue of debt securities and disclose the same in the offer document:
However, such minimum subscription limit shall not be less than seventy five per cent of the issue size.
- In the event of non-receipt of minimum subscription as specified above, all application moneys received in the public issue shall be refunded forthwith to the applicants, within twelve days from the date of the closure of the issue.

- In the event, there is a delay by the issuer in making the aforesaid refund, then the issuer shall refund the subscription amount along with interest at the rate of ten per cent per annum for the delayed period.

Utilization of issue proceeds

- The funds raised from public issue of debt securities shall be used only for projects that are specified under objects in the offer document.
- The proceeds of the issue shall be clearly earmarked for a defined project or a set of projects for which requisite approvals have been obtained from concerned authorities.
- The issuers shall maintain a bank account in which the amount raised from the issue shall be transferred immediately after the closure of the issue and such amount shall only be utilised for specified project(s). However, where the issuer is a Corporate Municipal Entity, the issue proceeds, net of issue expenses, shall be used only for onward lending to municipalities, as disclosed in the offer document.

Further, where the issuer is a corporate municipal entity, it shall maintain sufficient interest margin while onward lending to the municipalities, to meet its operating expenses and obligations.

- The issuer shall establish a separate project implementation cell and designate a project officer who shall not be below the rank of deputy commissioner, who shall monitor the progress of the project(s) and shall ensure that the funds raised are utilised only for the project(s) for which the debt securities were issued.

However, where the issuer is a corporate municipal entity, such requirement shall be complied by the Municipality which is being financed.

- Issuer's contribution for each project shall not be less than twenty per cent of the project costs, which shall be contributed from their internal resources or grants.

However, where the issuer is a corporate municipal entity, contribution of the concerned municipality, which is being financed by the corporate municipal entity, shall not be less than twenty per cent of the project costs, which shall be contributed from its internal resources or grants.

- The issuer shall disclose the schedule of implementation of the project in the offer document in a tabular form and the funds raised by the issuer shall be utilized in accordance with the said schedule.

Mandatory listing

An issuer desirous of making an offer of debt securities to the public shall make an application for listing to one or more recognised stock exchanges:

However, in case of issuer being corporate municipal entity, such an application shall be made in terms of sub-section (1) of section 40 of the Companies Act, 2013.

Conditions for listing of debt securities issued on private placement basis

An issuer may list its debt securities issued on private placement basis on a recognised stock exchange subject to the following conditions:

- (a) an issuer may issue general obligation bonds or revenue bonds;
- (b) accounts of municipality being the issuer, shall be prepared in accordance with National Municipal Accounts Manual or in accordance with similar Municipal Accounts Manual adopted by the respective State Government for at least three immediately preceding financial years;
- (c) no order or direction of restraint, prohibition or debarment by SEBI against the corporate municipal entity or its directors is in force;
- (d) the issuer, being a corporate municipal entity, has issued such debt securities in compliance with the provisions of Companies Act, 2013 and particularly section 42 of the Companies Act, 2013 and rules prescribed there under and other applicable laws;

- (e) the issuer shall not solicit or collect funds by issue of debt securities, except by way of private placement;
- (f) the minimum subscription amount per investor shall not be less than rupees twenty five lakh or such amount as may be specified by SEBI from time to time;
- (g) credit rating has been obtained in respect of such debt securities from at least one credit rating agency registered with SEBI;
- (h) the debt securities proposed to be listed are in dematerialized form;
- (i) the disclosures as provided in Schedule I of these regulations have been made.

Submission of accounts for Private Placement

Any issuer proposing to issue debt securities on private placement basis under SEBI (Issue and Listing of Debt Securities by Municipalities) Regulations, 2015, in the FY 2017-18, shall submit the following documents:

- a) Audited accounts for the financial years 2013-14, 2014-15 and 2015-16 in the information memorandum to the stock exchanges.
- b) For the immediately preceding FY i.e. FY 2016-17, the issuers shall submit the half yearly financial statements, as available (audited or unaudited) as on September 2016.

Although, the audited accounts for 2016-17 would have to be submitted within one year from the end of March 31, 2018 to stock exchanges where the debt securities have been listed. Such audited accounts would have to be displayed on the website of the recognised stock exchanges and the issuer. In addition, the issuers would be required to provide, on request, a copy (physical or electronic) of such audited accounts to its investors.

Trust deed

- A trust deed for securing the issue of debentures shall be executed by the issuer in favour of the independent trustee or debenture trustee, as applicable, within three months of the closure of the issue.
- The trust deed shall contain such clauses as may be prescribed in Schedule IV of the SEBI (Debenture Trustees) Regulations, 1993.

However, in case of private placement by a corporate municipal entity, the trust deed shall, in addition, contain such clauses as prescribed under section 71 of the Companies Act, 2013 and Companies (Share Capital and Debentures) Rules 2014.

- The trust deed shall not contain a clause which has the effect of:
 - (a) limiting or extinguishing the obligations and liabilities of the debenture trustees or the issuer in relation to any rights or interests of the investors;
 - (b) limiting or restricting or waiving the provisions of the Act, these regulations and circulars or guidelines issued by SEBI;
 - (c) indemnifying the debenture trustees or the issuer for loss or damage caused by their act of negligence or commission or omission.

Debenture redemption reserve

For the redemption of the debentures issued by a corporate municipal entity, the issuer shall create debenture redemption reserve in accordance with the provisions of the Companies Act, 2013 and the rules made thereunder.

Where the issuer is a corporate municipal entity and the issuer has defaulted in payment of interest on debt securities or redemption thereof or in creation of security as per the terms of the issue of debt securities, any distribution of dividend shall require approval of the debenture trustees.

Continuous listing conditions

- All the issuers making public issues of debt securities or seeking listing of debt securities issued on

private placement basis, shall comply with conditions of listing including continuous disclosure and other requirements specified by SEBI in general and those specified in Schedule V to these regulations.

- Where the issuer is corporate municipal entity, one-third of its Board shall comprise of independent directors, as defined in section 149 of the Companies Act, 2013.
- Every rating obtained by an issuer shall be periodically reviewed by the registered credit rating agency and any revision in the rating shall be promptly disclosed by the issuer to the stock exchange(s) where the debt securities are listed.
- In the event of credit rating being downgraded by two or more notches below the rating assigned at the time of issue, the issuer shall present to all bondholders, the reasons for fall in rating and the steps, if any, it intends to take to recover the rating.
- Any change in rating shall be promptly disseminated in such manner as the stock exchange where such securities are listed may determine from time to time.
- The issuer, the respective debenture trustees, wherever appointed, and stock exchanges shall disseminate all information and reports regarding debt securities including compliance reports filed by the issuers and the debenture trustees, if appointed, to the investors and the general public by placing them on their websites.
- The information referred shall also be placed on the websites, if any, of the debenture trustee, the issuer and the stock exchanges.

SEBI issued disclosures norms under regulation 23 of SEBI (Issue and Listing of Debt Securities by Municipalities) Regulations, 2015 ('ILDM Regulation'). All the issuers making public issues of debt securities or seeking listing of debt securities issued on private placement basis, shall comply with conditions of listing including continuous disclosure and other requirements specified by SEBI. The said disclosures, *inter-alia*, include disclosures for financial as well as non-financial information.

Trading and reporting of debt securities

- The debt securities issued to the public or on a private placement basis, which are listed in recognised stock exchanges, shall be traded and such trades shall be cleared and settled in recognised Clearing Corporation subject to conditions specified by SEBI.
- The trading lot for privately placed debt securities shall be rupees one lakh or such amount as may be specified by SEBI.
- In case of trades of debt securities which have been made over the counter, such trades shall be reported on a recognised stock exchange having a nationwide trading terminal or such other platform as may be specified by SEBI from time to time.
- The information in respect of issues such as issuer details, instrument details, ratings, rating migration, coupon, buyback, redemption details, shall be required to be reported to a common database with depositories or any other platform as may be specified by SEBI.

COMPLIANCES UNDER SEBI (LISTING OBLIGATIONS AND DISCLOSURE REQUIREMENTS) REGULATIONS, 2015

Obligation of Listed Entity which has listed its Non-Convertible Debt Securities

The Provisions of Chapter V of SEBI (LODR) Regulations, 2015 shall apply only to a listed entity which has listed its 'Non-Convertible Debt Securities' and/or 'Non-Convertible Redeemable Preference Shares' on a recognised stock exchange in accordance with SEBI (Issue and Listing of Debt Securities) Regulations, 2008 or SEBI (Issue and Listing of Non-Convertible Redeemable Preference Shares) Regulations, 2013 respectively.

The provisions of this chapter shall also be applicable to "perpetual debt instrument" and "perpetual non-cumulative preference share" listed by banks.

Sl. No.	Regulation No. of SEBI (LODR) Regulations, 2015	Subject	Particulars
1.	Regulation 50	Intimation to stock exchange(s)	<ul style="list-style-type: none"> • Prior intimation to the stock exchange(s) at least eleven working days before the date on and from which the interest on debentures and bonds, and redemption amount of redeemable shares or of debentures and bonds shall be payable. • Intimate the stock exchange(s), its intention to raise funds through new non-convertible debt securities or non-convertible redeemable preference shares it proposes to list either through a public issue or on private placement basis, prior to issuance of such securities. However, the above intimation may be given prior to the meeting of board of directors wherein the proposal to raise funds through new non convertible debt securities or non-convertible redeemable preference shares shall be considered. • Intimate to the stock exchange(s), at least two working days in advance, excluding the date of the intimation and date of the meeting, regarding the meeting of its board of directors, at which the recommendation or declaration of issue of non convertible debt securities or any other matter affecting the rights or interests of holders of non convertible debt securities or non convertible redeemable preference shares is proposed to be considered.
2.	Regulation 51	Disclosure of information having bearing on performance/ operation of listed entity and/or price sensitive information	<ul style="list-style-type: none"> • The listed entity shall promptly inform the stock exchange(s) of all information having bearing on the performance/operation of the listed entity, price sensitive information or any action that shall affect payment of interest or dividend of non-convertible preference shares or redemption of non convertible debt securities or redeemable preference shares. <i>Explanation.- The expression 'promptly inform', shall imply that the stock exchange must be informed as soon as practically possible and without any delay and that the information shall be given first to the stock exchange(s) before providing the same to any third party.</i> • The listed entity who has issued or is issuing non

			convertible debt securities and/or non-convertible redeemable preference shares shall make disclosures as specified in Part B of Schedule III.
3.	Regulation 52	Financial Results	<ul style="list-style-type: none"> The listed entity shall prepare and submit un-audited or audited financial results on a half yearly basis in the format as specified by SEBI within forty five days from the end of the half year to the recognised stock exchange(s). The listed entity shall comply with following requirements with respect to preparation, approval, authentication and publication of annual and half-yearly financial results: <ul style="list-style-type: none"> (a) Un-audited financial results shall be accompanied by limited review report prepared by the statutory auditors of the listed entity or in case of public sector undertakings, by any practising Chartered Accountant, in the format as specified by SEBI. However, if the listed entity intimates in advance to the stock exchange(s) that it shall submit to the stock exchange(s) its annual audited results within sixty days from the end of the financial year, un-audited financial results for the last half year accompanied by limited review report by the auditors need not be submitted to stock exchange(s). (b) Half-yearly results shall be taken on record by the board of directors and signed by the managing director / executive director. (c) The audited results for the year shall be submitted to the recognised stock exchange(s) in the same format as is applicable for half-yearly financial results. (d) If the listed entity opts to submit un-audited financial results for the last half year accompanied by limited review report by the auditors, it shall also submit audited financial results for the entire financial year, as soon as they are approved by the board of directors. (e) Modified opinion(s) in audit reports that have a bearing on the interest payment/ dividend payment pertaining to non-convertible redeemable debentures/ redemption or principal repayment capacity of the listed entity shall be appropriately and adequately addressed by the board of directors while publishing the accounts for the said period. The annual audited financial results shall be submitted along with the annual audit report and statement on Impact of Audit Qualifications (applicable only) for audit report with modified opinion.

			<ul style="list-style-type: none"> • The statement on Impact of Audit Qualifications for audit report with modified opinion and the accompanying annual audit report submitted shall be reviewed by the stock exchange(s) and the Qualified Audit Report Review Committee in the manner specified in Schedule VIII. • The listed entity, while submitting half yearly / annual financial results, shall disclose the following line items along with the financial results: <ul style="list-style-type: none"> (a) credit rating and change in credit rating (if any); (b) asset cover available, in case of non convertible debt securities; (c) debt-equity ratio; (d) previous due date for the payment of interest/ dividend for non-convertible redeemable preference shares/ repayment of principal of non-convertible preference shares /non convertible debt securities and whether the same has been paid or not; and, (e) next due date for the payment of interest/ dividend of non-convertible preference shares /principal along with the amount of interest/ dividend of non-convertible preference shares payable and the redemption amount; (f) debt service coverage ratio; (g) interest service coverage ratio; (h) outstanding redeemable preference shares (quantity and value); (i) capital redemption reserve/debenture redemption reserve; (j) net worth; (k) net profit after tax; (l) earnings per share : <p>However, the requirement of disclosures of debt service coverage ratio, asset cover and interest service coverage ratio shall not be applicable for banks or non banking financial companies registered with the Reserve Bank of India. Further, the disclosure requirement mentioned above shall not be applicable in case of unsecured debt instruments issued by regulated financial sector entities eligible for meeting capital requirements as specified by respective regulators.</p>
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			<ul style="list-style-type: none"> • While submitting the information required, the listed entity shall submit to stock exchange(s), a certificate signed by debenture trustee that it has taken note of the contents. • The listed entity shall submit to the stock exchange on a half yearly basis along with the half yearly financial results, a statement indicating material deviations, if any, in the use of proceeds of issue of non convertible debt securities and non-convertible redeemable preference shares from the objects stated in the offer document. • The listed entity shall, within two calendar days of the conclusion of the meeting of the board of directors, publish the financial results and statement, in at least one English national daily newspaper circulating in the whole or substantially the whole of India.
4.	Regulation 53	Annual Report	<p>The annual report of the listed entity shall contain disclosures as specified in Companies Act, 2013 along with the following:</p> <ul style="list-style-type: none"> (a) audited financial statements i.e. balance sheets, profit and loss accounts etc; (b) cash flow statement presented only under the indirect method as prescribed in Accounting Standard-3/ Indian Accounting Standard 7, mandated under Section 133 of the Companies Act, 2013 read with relevant rules framed thereunder or by the Institute of Chartered Accountants of India, whichever is applicable; (c) auditors report; (d) directors report; (e) name of the debenture trustees with full contact details; (f) related party disclosures as specified in Para A of Schedule V.
5.	Regulation 54	Asset Cover	<ul style="list-style-type: none"> • In respect of its listed non-convertible debt securities, the listed entity shall maintain hundred per cent asset cover sufficient to discharge the principal amount at all times for the non-convertible debt securities issued. • The listed entity shall disclose to the stock exchange in quarterly, half-yearly, year-to-date and annual financial statements, as applicable, the extent and nature of security created and maintained with respect to its secured listed non-convertible debt securities. <p>However, above mentioned requirements shall not be</p>

			applicable in case of unsecured debt securities issued by regulated financial sector entities eligible for meeting capital requirements as specified by respective regulators.
6.	Regulation 55	Credit Rating	<ul style="list-style-type: none"> Each rating obtained by the listed entity with respect to non-convertible debt securities shall be reviewed at least once a year by a credit rating agency registered by SEBI.
7.	Regulation 56	Documents and Intimation to Debenture Trustees	<ul style="list-style-type: none"> The listed entity shall forward the following to the debenture trustee promptly: <ul style="list-style-type: none"> (a) a copy of the annual report at the same time as it is issued along with a copy of certificate from the listed entity's auditors in respect of utilisation of funds during the implementation period of the project for which the funds have been raised. However, in the case of debentures or preference shares issued for financing working capital or general corporate purposes or for capital raising purposes the copy of the auditor's certificate may be submitted at the end of each financial year till the funds have been fully utilised or the purpose for which these funds were intended has been achieved. (b) a copy of all notices, resolutions and circulars relating to – <ul style="list-style-type: none"> (i) new issue of non convertible debt securities at the same time as they are sent to shareholders/holders of non convertible debt securities; (ii) the meetings of holders of non-convertible debt securities at the same time as they are sent to the holders of non convertible debt securities or advertised in the media including those relating to proceedings of the meetings; (c) intimations regarding : <ul style="list-style-type: none"> (i) any revision in the rating; (ii) any default in timely payment of interest or redemption or both in respect of the non convertible debt securities; (iii) failure to create charge on the assets; (d) a half-yearly certificate regarding maintenance of hundred percent asset cover in respect of listed non convertible debt securities, by either a practicing company secretary or a practicing chartered accountant, along with the half yearly financial results. However, submission of such half yearly certificates is not applicable in cases where a listed

			<p>entity is a bank or non banking financial companies registered with Reserve Bank of India or where bonds are secured by a Government guarantee.</p> <ul style="list-style-type: none"> The listed entity shall forward to the debenture trustee any such information sought and provide access to relevant books of accounts as required by the debenture trustee. The listed entity may, subject to the consent of the debenture trustee, send the information, in electronic form/fax.
8.	Regulation 57	Other submissions to stock exchange(s)	<ul style="list-style-type: none"> The listed entity shall submit a certificate to the stock exchange within two days of the interest or principal or both becoming due that it has made timely payment of interests or principal obligations or both in respect of the non convertible debt securities. The listed entity shall provide an undertaking to the stock exchange(s) on annual basis stating that all documents and intimations required to be submitted to Debenture Trustees in terms of Trust Deed and SEBI (Issue and Listing of Debt Securities) Regulations, 2008 have been complied with. The listed entity shall forward to the stock exchange any other information in the manner and format as specified by SEBI from time to time.
9.	Regulation 58	Documents and information to holders of non-convertible debt securities and non-convertible preference shares	<p>The listed entity shall send the following documents to holders of non-convertible debt securities :</p> <ul style="list-style-type: none"> Hard copies of full annual reports to those, who request for the same. Half yearly communication Notice of all meetings specifically stating that the provisions for appointment of proxy as mentioned in Section 105 of the Companies Act, 2013, shall be applicable for such meeting. Proxy forms which shall be worded in such a manner that holders of these securities may vote either for or against each resolution.
10.	Regulation 59	Structure of non convertible debt securities and non-convertible redeemable preference shares	<ul style="list-style-type: none"> The listed entity shall not make material modification without prior approval of the stock exchange(s) where the non convertible debt securities or non-convertible redeemable preference shares, as applicable, are listed, to : <ul style="list-style-type: none"> (a) the structure of the debenture in terms of coupon, conversion, redemption, or otherwise. (b) the structure of the non-convertible redeemable preference shares in terms of dividend of non-

			<p>convertible preference shares payable, conversion, redemption, or otherwise.</p> <p>The approval of the stock exchange shall be made only after:</p> <p>(a) approval of the board of directors and the debenture trustee in case of non-convertible debt securities and</p> <p>(b) after complying with the provisions of Companies Act, 2013 including approval of the consent of requisite majority of holders of that class of securities.</p>
11	Regulation 60	Record Date	<ul style="list-style-type: none"> The listed entity shall fix a record date for purposes of payment of interest, dividend and payment of redemption or repayment amount or for such other purposes as specified by the stock exchange. The listed entity shall give notice in advance of at least seven working days (excluding the date of intimation and the record date) to the recognised stock exchange(s) of the record date or of as many days as the stock exchange(s) may agree to or require specifying the purpose of the record date.
12.	Regulation 61	Terms of non-convertible debt securities and non-convertible redeemable preference shares	<ul style="list-style-type: none"> The listed entity shall ensure timely payment of interest or dividend of non-convertible redeemable preference shares or redemption payment. However, the listed entity shall not declare or distribute any dividend wherein it has defaulted in payment of interest on debt securities or redemption thereof or in creation of security as per the terms of the issue of debt securities. However, the requirement of the regulation shall not be applicable in case of unsecured debt securities issued by regulated financial sector entities eligible for meeting capital requirements as specified by respective regulators. The listed entity shall not forfeit unclaimed interest/dividend and such unclaimed interest/dividend shall be transferred to the 'Investor Education and Protection Fund' set up as per Section 125 of the Companies Act, 2013. Unless the terms of issue provide otherwise, the listed entity shall not select any of its listed securities for redemption otherwise than pro rata basis or by lot. The listed entity shall comply with the requirements for transfer of securities including procedural requirements specified in Schedule VII.
13.	Regulation 62	Website	<ul style="list-style-type: none"> The listed entity shall maintain a functional website containing the following information about the listed entity:-

			<p>(a) details of its business;</p> <p>(b) financial information including complete copy of the annual report including balance sheet, profit and loss account, directors report etc;</p> <p>(c) contact information of the designated officials of the listed entity who are responsible for assisting and handling investor grievances;</p> <p>(d) email address for grievance redressal and other relevant details;</p> <p>(e) name of the debenture trustees with full contact details;</p> <p>(f) the information, report, notices, call letters, circulars, proceedings, etc. concerning non-convertible redeemable preference shares or non convertible debt securities;</p> <p>(g) all information and reports including compliance reports filed by the listed entity;</p> <p>(h) information with respect to the following events:</p> <ul style="list-style-type: none"> (i) default by issuer to pay interest on or redemption amount; (ii) failure to create a charge on the assets; (iii) revision of rating assigned to the non convertible debt securities: <ul style="list-style-type: none"> • The listed entity may also issue a press release with respect to the events specified in the above para. • The listed entity shall ensure that the contents of the website are correct and updated at any given point of time.
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II. Obligations of Listed Entity which has listed its specified securities and either non-convertible debt securities or both

Applicability

Entity which has listed its 'specified securities' and 'non-convertible debt securities' or 'non-convertible redeemable preference shares' or both on any recognised stock exchange, shall be bound by the provisions in Chapter IV and additionally comply with Chapter V of these regulations.

However, the listed entity which has submitted any information to the stock exchange in compliance with the disclosure requirements under Chapter IV of these regulations, need not re-submit any such information under the provisions of this regulations without prejudice to any power conferred on SEBI or the stock exchange or any other authority under any law to seek any such information from the listed entity. Further, the listed entity, which has satisfied certain obligations in compliance with other chapters, shall not separately satisfy the same conditions under chapter VI.

Delisting (Regulation 64)

- In the event specified securities of the listed entity are delisted from the stock exchange, the listed entity shall comply with all the provisions in Chapter V of these regulations.
- In the event that non-convertible debt securities and non-convertible redeemable preference shares' of the listed entity do not remain listed on the stock exchange, the listed entity shall comply with all the provisions in Chapter IV of these regulations.

III. Obligations of listed entity which has listed its securitised debt instruments

The provisions of chapter VIII of SEBI (LODR) Regulations shall apply to Special Purpose Distinct Entity issuing securitised debt instruments and the trustees of Special Purpose Distinct Entity shall ensure compliance with each of the provisions of these regulations.

Sl. No.	Regulation No. of SEBI (LODR) Regulations, 2015	Subject	Particulars
1.	Regulation 82	Intimation and filings with stock exchange(s)	<ul style="list-style-type: none"> • Prior intimation to the Stock exchange, of its intention to issue new securitized debt instruments either through a public issue or on private placement basis. • Intimation to the stock exchange(s), at least two working days in advance, excluding the date of the intimation and date of the meeting, regarding the meeting of its board of trustees, at which the recommendation or declaration of issue of securitized debt instruments or any other matter affecting the rights or interests of holders of securitized debt instruments is proposed to be considered. • Submission of such statements, reports or information including financial information pertaining to Schemes to stock exchange within seven days from the end of the month/ actual payment date, either by itself or through the servicer, on a monthly basis in the format as specified by SEBI from time to time. However, where periodicity of the receivables is not monthly, reporting shall be made for the relevant periods. • To provide the stock exchange, either by itself or through the servicer, loan level information, without disclosing particulars of individual borrowers, in manner specified by stock exchange.
2.	Regulation 83	Disclosure of information	<ul style="list-style-type: none"> • To promptly inform the stock exchange(s) of all information having bearing on the performance/ operation of the listed entity and price sensitive information. • To make the disclosures specified in Part D of Schedule III.

3.	Regulation 84	Credit Rating	<ul style="list-style-type: none"> • Every rating obtained by the listed entity with respect to securitised debt instruments shall be periodically reviewed, preferably once a year, by a credit rating agency registered by SEBI. • Any revision in rating(s) shall be disseminated by the stock exchange(s).
4.	Regulation 85	Information to Investors	<ul style="list-style-type: none"> • To provide either by itself or through the servicer, loan level information without disclosing particulars of individual borrower to its investors. • To provide information regarding revision in rating as a result of credit rating done periodically to its investors. • The information may be sent to investors in electronic form/fax if so consented by the investors. • To display the email address of the grievance redressal division and other relevant details prominently on its website and in the various materials / pamphlets/ advertisement campaigns initiated by it for creating investor awareness.
5.	Regulation 86	Terms of Securitized Debt Instruments	<ul style="list-style-type: none"> • To ensure that no material modification shall be made to the structure of the securitized debt instruments in terms of coupon, conversion, redemption, or otherwise without prior approval of the recognised stock exchange(s) and the listed entity shall make an application to the recognised stock exchange(s) only after the approval by Trustees. • To ensure timely interest/ redemption payment. • To ensure that where credit enhancement has been provided for, it shall make credit enhancement available for listed securitized debt instruments at all times. • The listed entity shall not forfeit unclaimed interest and principal and such unclaimed interest and principal shall be, after a period of seven years, transferred to the Investor Protection and Education Fund established under the SEBI (Investor Protection and Education Fund) Regulations, 2009. • Not to select any of its listed securitized debt instruments for redemption otherwise than on pro rata basis or by lot and shall promptly submit to the recognised stock exchange(s) the details thereof. • To remain listed till the maturity or redemption of securitised debt instruments or till the same are delisted as per the procedure laid down by SEBI. However, these provisions shall not restrict the right of the recognised stock exchange(s) to delist, suspend or remove the

			securities at any time and for any reason which the recognised stock exchange(s) considers proper in accordance with the applicable legal provisions.
6.	Regulation 87	Record Date	<ul style="list-style-type: none"> To fix a record date for payment of interest and payment of redemption or repayment amount or for such other purposes as specified by the recognised stock exchange(s). To give notice in advance of atleast seven working days (excluding the date of intimation and the record date) to the recognised stock exchange(s) of the record date or of as many days as the Stock Exchange may agree to or require specifying the purpose of the record date.

IV. Obligations of Listed Entity which has listed its Convertible Debt Instruments

For Convertible Debt Instruments, Chapter III along with Chapter IV of SEBI (LODR) Regulations is applicable.

As these both Chapters are also applicable to equity shares, the compliance part is discussed under the Lesson Listing and Delisting of securities of the study material.

Listing of NCRPS/ NCDs through a Scheme of Arrangement

Listing of Non-Convertible Redeemable Preference Shares (NCRPS) / Non-Convertible Debentures (NCDs) through a Scheme of Arrangement which established the obligations with respect to Scheme of Arrangement on Listed Entities and Stock Exchange(s) in regulation 11, 37 and 94 of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015.

In cases where NCRPS/NCDs are issued, in lieu of specified securities, vide a scheme of arrangement and where such NCRPS/NCDs are proposed to be listed on recognized stock exchanges, the listed entity shall additionally comply with the requirements of the new norms as specified below :

1. Eligibility for seeking listing of NCRPS/ NCDs

A listed entity which has listed its specified securities may seek listing of NCRPS/NCDs issued pursuant to a scheme of arrangement only in case where the listed entity is a part of such scheme of arrangement and such NCRPS/NCDs are issued to the holders of specified securities of such listed entity. Such conditions may broadly include the following:

- A listed entity, which has listed its specified securities, (demerged entity) demerges a unit and transfers the same to another entity (resultant entity), and the resultant entity issues NCRPS/NCDs to the holders of the specified securities of listed entity (i.e. demerged entity) as a consideration under the scheme of arrangement.
- A listed entity, which has listed its specified securities, (amalgamating entity) is merged with another entity (amalgamated entity), and the amalgamated entity issues NCRPS/NCDs to the holders of the specified securities of listed entity (i.e. amalgamating entity) as a consideration under the scheme of arrangement.

However, if the same series of securities are also allotted to other investors (other than the allotment done to the holders of listed specified securities as per the scheme of arrangement) then such securities would not be eligible for listing.

2. Tenure/ Maturity

The minimum tenure of the NCRPS/NCDs shall be one year.

3. Credit Rating

The NCRPS/NCDs have been assigned minimum such credit rating, if any, specified for public issue of NCRPS under SEBI (Issue and Listing of Non-Convertible Redeemable Preference Shares) Regulations, 2013 or for public issue of NCDs in terms of SEBI (Issue and Listing of Debt Securities) Regulations, 2008, as the case may be by a credit rating agency registered with SEBI.

4. Valuation Report

Valuation of the underlying NCRPS/ NCDs issued pursuant to the scheme of arrangement shall be included in the valuation report.

5. Disclosures in the Scheme of Arrangement

Various documents including face value and price, terms of payment of dividends coupon including frequency, credit rating, maturity, details about terms of redemption, amount, date, early redemption scenarios, other embedded features (put option, call option, dates, notification times, etc), other terms of instruments (i.e. term sheet) and any other information/details pertinent for the investors that need to be disclosed in Draft Scheme of Arrangement.

6. Other Conditions which would be required to be followed are as under

The issue of NCRPS/NCDs shall be in compliance with all the applicable provisions of the Companies Act, 2013 and SEBI (Issue and Listing of Debt Securities) Regulations, 2008 including the provisions related to creation and maintenance of Capital Redemption Reserve/Debenture Redemption Reserve, appointment of Debenture Trustee and create an appropriate charge or security. All such NCRPS/NCDs shall be issued in dematerialised form only.

7. Additional conditions to be complied after the Scheme is sanctioned by the Hon'ble High Court / NCLT and at the time of making application for relaxation under Sub-rule (7) of rule 19 of the Securities Contracts (Regulation) Rules, 1957

The application for relaxation under Sub-rule (7) of rule 19 of SCRR for listing of NCRPS/ NCDs shall include a detailed compliance report, duly certified by the Company Secretary and the Managing Director.

LESSON ROUND UP

- Debt markets are markets for the issuance, trading and settlement in fixed income securities of various types and features. Fixed income securities can be issued by almost any legal entity like central and state governments, public bodies, statutory corporations, banks and institutions and corporate bodies.
- The debt market in India comprises mainly of two segments viz., the Government securities market consisting of Central and State Governments securities, Zero Coupon Bonds (ZCBs), Floating Rate Bonds (FRBs), T-Bills and the Corporate securities market consisting of FI bonds, PSU bonds, and Debentures/Corporate bonds.
- Investors in debt market are the entities who invest in such fixed income instruments. The investors in such instruments are generally Banks, Financial Institutions, Mutual Funds, Insurance Companies, Provident Funds etc.
- Primary dealers (PDs) act as underwriters in the primary market, and as market makers in the secondary market. PDs underwrite a portion of the issue of government security that is floated for a pre-determined amount.

- Brokers play an important role in secondary debt market by bringing together counterparties and negotiating terms of the trade. It is through them that the trades are entered on the stock exchanges.
- Issue and listing of non-convertible debt securities, whether issued to the public or privately based, are required to be made in accordance with SEBI (Issue and Listing of Debt Securities) Regulations, 2008 and issue of convertible debt securities either partially or fully or optionally area required to be made in accordance with SEBI (ICDR) Regulations, 2009.
- Securitised debt instruments are regulated by the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002, SEBI (Public Offer and Listing of Securitized Debt Instruments) Regulations, 2008 for listing on stock exchanges and the Securitization Companies and Reconstruction Companies (Reserve Bank) Guidelines and Directions, 2003.
- SEBI (Issue and Listing of Debt Securities by Municipality) Regulations, 2015 was notified by SEBI on July 15, 2015. The regulations provide for public issuance and listing of privately placed municipal bonds and also provides for disclosure requirements to be made by the prospective issuers.
- SEBI notified the SEBI (Listing Obligations and Disclosure Requirement) Regulations, 2015 (Listing Regulations) on September 02, 2015 effective from December 01, 2015 for various types of listed entities.

GLOSSARY

Indenture	Agreement between lender and borrower which details specific terms of the bond issuance. Specifies legal obligations of bond issuer and rights of the bondholder. Document spelling out the specific terms of a bond as well as the rights and responsibilities of both the issuer of the security and the holder.
Originator	It means the assignor of debt or receivables to a special purpose distinct entity for the purpose of securitisation.
Real Time Gross Settlement (RTGS)	Concept designed to achieve sound risk management in the settlement of interbank payments. Transactions are settled across accounts held at the Central Bank on a continuous gross basis where settlement is immediate, final and irrevocable.
Special Purpose Distinct Entity (SPDE)	SPDE means a trust which acquires debt or receivables out of funds mobilized by it by issuance of securitised debt instruments through one or more schemes.
Ways and Means Advances (WMA)	It is a mechanism used by RBI under its credit policy to the State, banking with it to help them to tide over temporary mismatches in the cash flow of their receipts and payment.

SELF TEST QUESTIONS

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation.)

1. The debt market in India comprises mainly of two segments viz., the Government securities market and the Corporate securities market – Discuss.
2. Explain roll over of non-convertible portion of partly convertible debt instruments under SEBI (ICDR) Regulations, 2009.
3. Explain the Regulatory Framework of Debt Market in India.
4. Give an overview of various debt market instruments in India.
5. Briefly explain the provisions with respect to minimum subscription in case of public issue of Municipal Bonds.

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Lesson 6

Money Market

LESSON OUTLINE

- Introduction
- Features of Money Market
- Money Market vs. Capital Market
- Growth of Money Market
- Structure and Institutional Development
- Money Market Instruments
- Treasury Bills
- Certificates of Deposits
- Inter-Corporate Deposits
- Commercial Bills
- Commercial Paper
- Factoring
- Bills Rediscounting
- LESSON ROUND UP
- GLOSSARY
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

The money market deals in the lending and borrowing of short term finance varying from one year or less. The main credit instrument of the money market are call money, treasury bills, commercial bills, commercial papers and bills of exchange. Important institutions operating in the money market are central banks, commercial banks, acceptance house, non-banking financial institutions, bill brokers etc. The money market meets the short-term credit needs of business, it provides working capital to the industrialists.

Keeping this in view, this lesson will explain the basic understanding of money market, its feature and structures, various instruments available in the money market and difference between the money market and capital market are explained.

INTRODUCTION

Money market is a very important segment of a financial system. Monetary assets of short-term nature up to one year and financial assets that are close substitutes for money are dealt in the money market. Money market instruments have the characteristics of liquidity (quick conversion into money), minimum transaction cost and no loss in value. Excess funds are deployed in the money market, which in turn is availed of to meet temporary shortages of cash and other obligations. Money market provides access to providers and users of short-term funds to fulfill their investments and borrowings requirements respectively at an efficient market clearing price. It performs the crucial role of providing an equilibrating mechanism to even out short-term liquidity, surpluses and deficits and in the process, facilitates the conduct of monetary policy. The money market is one of the primary mechanism through which the Central Bank influences liquidity and the general level of interest rates in an economy. The Bank's interventions to influence liquidity serve as a signaling-device for other segments of the financial system.

The money market functions as a wholesale debt market for low-risk, highly liquid, short term instruments. Funds are available in this market for periods ranging from a single day upto a year. Mostly government, banks and financial institutions dominate this market. It is a formal financial market that deals with short-term fund management.

Though there are a few types of players in money market, the role and the level of participation by each type of player differs largely.

Government is an active player in the money market and in most of the economies; it constitutes the biggest borrower in this market. Both, Government securities (G-secs) and Treasury bill (T-bill) is a security issued by RBI on behalf of the Government of India to meet the latter's borrowing for financing fiscal deficit. Apart from functioning as a banker to the government, the Central Bank (RBI) also regulates the money market and issues guidelines to govern the money market operations.

Another dominant player in the money market is the banking industry. Banks mobilize deposits of savers in lending to investors of the economy. This process is known as credit creation. However, banks are not allowed to lent out the entire amount for extending credit for investment. In order to promote certain prudential norms for healthy banking practices, most of the developed economies require all commercial banks to maintain minimum liquid and cash reserves in form of Statutory Liquidity Ratio (SLR) and Cash Reserve Ratio (CRR) framed under the policies of Central Banks. The banks are required to ensure that these reserve requirements are met before directing deposits on their credit plans. If banks fall short of these statutory reserve requirements, the deficit amount can be raised using the money market.

Other institutional players like financial institutions, corporates, mutual funds (MFs), Foreign institutional investors (FIIs) etc. also transact in money market to fulfill their respective short term finance deficits and short falls. However, the degree of participation of these players depends largely on the regulations formulated by the regulating authorities in an economy. For instance, the level of participation of the FIIs in the Indian money market is restricted to investment in government securities only.

FEATURES OF MONEY MARKET

The money market is a wholesale market where the volumes of transactions is very large and is settled on a daily basis. Trading in the money market is conducted over the telephone, followed by written confirmation through e-mails, texts from the borrowers and lenders.

There are a large number of participants in the money market: commercial banks, mutual funds, investment institutions, financial institutions and finally the Reserve Bank of India. The bank's operations ensure that the liquidity and short-term interest rates are maintained at levels consistent with the objective of maintaining price

and exchange rate stability. The Central Bank occupies a strategic position in the money market. The money market can obtain funds from the central bank either by borrowing or through sale of securities. The bank influences liquidity and interest rates by open market operations, REPO transactions changes in Bank Rate, Cash Reserve Requirements and by regulating access to its accommodation. A well-developed money market contributes to an effective implementation of the monetary policy. It provides:

1. A balancing mechanism for short-term surpluses and deficiencies.
2. A focal point of Central Bank intervention for influencing liquidity in the economy, and
3. A reasonable access to the users of short-term funds to meet their requirements at realistic/reasonable price or cost.

MONEY MARKET Vs. CAPITAL MARKET

The money market possesses different operational features as compared to capital market. Money market is distinguished from capital market on the basis of the maturity period, credit instruments and the institutions:

Point of Distinction	Money Market	Capital Market
Maturity Period	It primarily deals in the lending and borrowing of short-term finance varying for one year or less.	It primarily deals in the lending and borrowing of long-term finance for more than one year.
Credit Instruments	The main credit instruments of the money market are call money, treasury bills, commercial bills, commercial papers, and bills of exchange.	The main instruments used in the capital market are stocks, shares, debentures, bonds, corporate deposits etc.
Institutions	Central Banks, Commercial Banks, Non-Banking Financial Institutions, Bill Brokers, etc.	Stock Exchanges, Commercial Banks, Insurance Companies and mortgage banks etc.
Market Regulation	Money Market are closely regulated	Capital Market are not much regulated.
Risk and Liquidity	Relatively lower risk and high liquidity.	Higher risk and lower liquidity.
Purpose of Loan	It meets the short-term credit needs of business; it provides working capital to the industrialists.	It caters the long-term credit needs of the industrialists and provides fixed capital to buy land, machinery, etc.

GROWTH OF MONEY MARKET

Post reforms period in India has witnessed tremendous growth of the Indian money markets. Banks and other financial institutions have been able to meet the high expectations of short term funding of important sectors like the industry, services and agriculture. Functioning under the regulation and control of the Reserve Bank of India (RBI), the Indian money markets have also exhibited the required maturity and resilience over the years.

The organization and structure of the money market has undergone a sea change in the last decade in India. This was accompanied by a growth in quantitative terms also.

Up to 1987, the money market consist of 6 facts :

1. Call Money Market;
2. Inter Bank Term Deposit/Loan Market;
3. Participation Certificate Market;
4. Commercial Bills Market;
5. Treasury Bills Market; and
6. Inter-corporate Market.

The market had 3 main deficiencies:

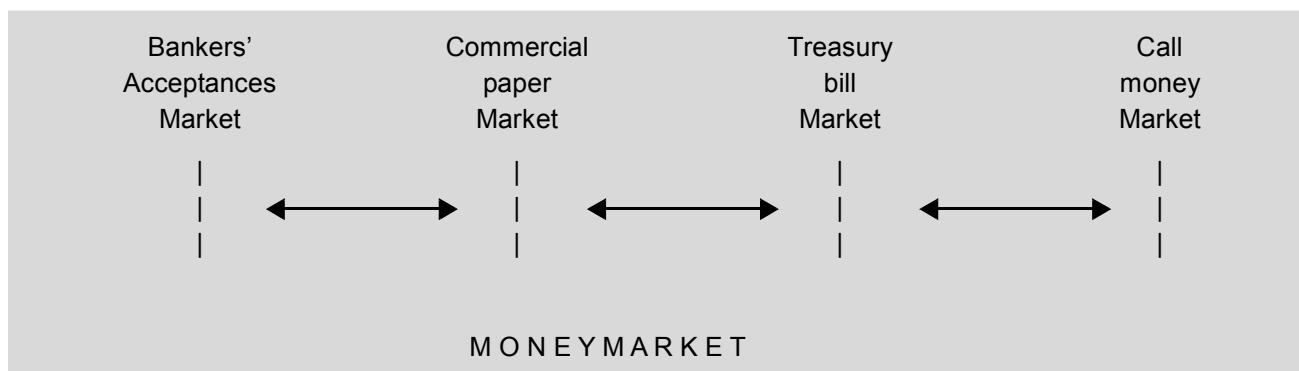
1. It had a very narrow base with RBI, Banks, LIC and UTI as the only participants lending funds while the borrowers were large in number;
2. There were only few money market instruments.
3. The interest rates were not market determined but were controlled either by RBI or by a voluntary agreement between the participants through the Indian Banks Association (IBA).

To set right these deficiencies, the recommendations of Chakravorthy Committee (1985) and the Vaghul Committee (1987) laid foundation for systematic development of the Indian Money Market. The implementation of the suggestions of the respective committees has widened and deepened the market considerably by increasing the number of participants and instruments and introducing market determined rates as against the existing administered or volunteered interest rates.

Further, an active secondary market for dealings of money market instrument was created which positively impacted the liquidity of these instruments. For this purpose, the Discount and Finance House of India Limited (DFHI) was formed as an autonomous financial intermediary in April, 1988 to embellish the short-term liquidity imbalances and to develop an active secondary market for the trading of instruments of the money market. The DFHI plays the role of a market maker in money market instruments. With the relaxation of the regulatory framework and the arrival of new instruments and participants, DFHI occupies a key role in ushering a more active and de-regulated money market.

STRUCTURE AND INSTITUTIONAL DEVELOPMENT

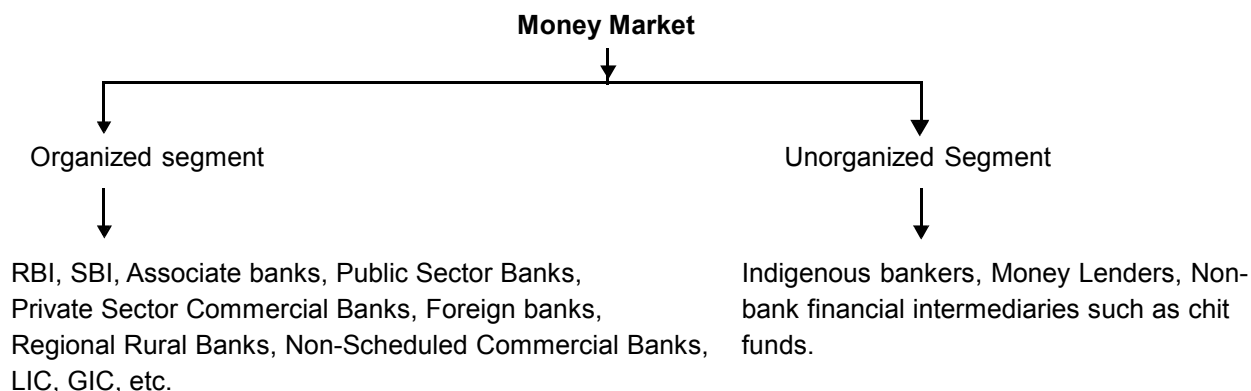
The following diagram depicts the important segments and inter-relation in the money market:



The Indian Money Market consists of two types of segments: an organized segment and an unorganized segment. In the unorganized segment, interest rates are much higher than that in the organized segment.

The organized segment consists of the Reserve Bank of India, State Bank of India with its associate Banks, Public Sector Banks, Private Sector Commercial Banks including Foreign Banks, Regional Rural Banks, Non-Scheduled Commercial Banks, apart from Non-banking Financial Intermediaries such as LIC, GIC etc.

The unorganized segment essentially consists of indigenous bankers, money lenders and other non-bank financial intermediaries such as Chit Funds. For these institutions there is no clear cut demarcation between short-term and long-term and between a genuine trade bill and mere financial accommodation. The share of the unorganized sector in providing trade finance has greatly diminished after the Nationalization of Bank and expansion thereof into the length and breadth of the country.



MONEY MARKET INSTRUMENTS

TREASURY BILLS

Treasury Bills are money market instruments issued by RBI to finance the short term requirements of the Government of India. These are discounted securities and thus are issued at a discount to face value. The return to the investor is the difference between the maturity value and issue price.

In the short term category of investment instruments, the treasury bill carry the lowest risk. RBI issues these at a prefixed date and of a fixed amount.

Treasury Bills are very useful instruments to deploy short term surpluses depending upon the availability and requirement. Even funds which are kept in current accounts can be deployed in treasury bills to maximise returns. Banks do not pay any interest on fixed deposits of less than 15 days, or balances maintained in current accounts, whereas treasury bills can be purchased for any number of days depending on the requirements. This helps in deployment of idle funds for very short periods as well. Further, since every week there is a 91 days treasury bills maturing and every fortnight a 364 days treasury bills maturing, one can purchase treasury bills of different maturities as per requirements so as to match with the respective outflow of funds. At times when the liquidity in the economy is tight, the returns on treasury bills are much higher as compared to bank deposits even for longer term. Besides, better yields and availability for very short tenors, another important advantage of treasury bills over bank deposits is that the surplus cash can be invested depending upon the staggered requirements.

Example

Suppose party A has a surplus cash of ₹ 200 crore to be deployed in a project. However, it does not require the funds at one go but requires them at different points of time as detailed below:

Funds Available as on 1.1.2017	₹ 200 crore
Deployment in a project	₹ 200 crore
As per the requirements	
06.1.2017	₹ 50 crore
13.1.2017	₹ 20 crore

158 EP-CM&SL

02.2.2017

₹ 30 crore

08.2.2017

₹ 100 crore

Out of the above funds and the requirement schedule, the party has following two options for effective cash management of funds:

Option I

Invest the cash not required within 15 days in bank deposits

The party can invest a total of ₹ 130 crore only, since the balance ₹ 70 crores is required within the first 15 days. Assuming a rate of return of 6% paid on bank deposits for a period of 31 to 45 days, the interest earned by the company works out to ₹ 76 lacs approximately.

Option II

Invest in Treasury Bills of various maturities depending on the funds requirements

The party can invest the entire ₹ 200 crore in treasury bills as treasury bills of even less than 15 days maturity are also available. The return to the party by this deal works out to around ₹ 125 lacs, assuming returns on Treasury Bills in the range of 8% to 9% for the above periods.

There are four types of treasury bills :

(a) 14-days T bill

The Maturity is in 14 days. Its auction is on every Friday of every week. The notified amount for this auction is ₹ 100 crores.

(b) 91-days T bill

The Maturity is in 91 days. Its auction is on every Friday of every week. The notified amount for this auction is ₹ 100 crores.

(c) 182-days T bill

The Maturity is in 182 days. Its auction is on every alternate Wednesday (which is not a reporting week). The notified amount for this auction is ₹ 100 crores.

(d) 364-days T bill

The Maturity is in 364 days. Its auction is on every alternate Wednesday (which is a reporting week). The notified amount for this auction is ₹ 500 crores.

A considerable part of the government's borrowings is financed through T-bills of various maturities. Based on the bids received at the auctions, RBI decides the cut off yield and accepts all bids below this yield.

The usual investors in these instruments are banks who invest not only to invest their short-term surpluses but also to get benefitted for maintaining the Statutory Liquidity Ratio (SLR) requirements in T-bills is reckoned for the purpose of statutory reserves. FIIs so far have not been allowed to invest in this instrument.

These T-bills which are issued at a discount can be traded in the market. Most of the time, unless the investor requests specifically, these are issued not as securities but as entries in the Subsidiary General Ledger (SGL) which is maintained by RBI. The transactions cost on T-bill are non-existent and trading is considerably high in each bill, immediately after its issue and immediately before its redemption.

The yield on T-bills is dependent on the rates prevalent on other investment avenues open for investors. For instance, low yield on T-bills as a result of high liquidity in banking system due to by low call rates, would divert the funds from T-bills market to other markets. This would particularly be so, if banks already hold the minimum stipulated amount of SLR in government instrument.

BENEFITS OF INVESTMENT IN TREASURY BILLS

- (a) No tax deducted at source
- (b) Zero default risk being sovereign paper
- (c) Highly liquid money market instrument
- (d) Better returns especially in the short term
- (e) Transparency
- (f) Simplified settlement
- (g) High degree of tradeability and active secondary market facilitates meeting unplanned fund requirements.

FEATURES OF TREASURY BILLS

(a) Form

The treasury bills are issued in the form of promissory note in physical form or by credit to Subsidiary General Ledger (SGL) account or Gilt account in dematerialized form.

(b) Minimum Amount of Bids

Bids for treasury bills are to be made for a minimum amount of ₹ 25000/- only and in multiples thereof.

(c) Eligibility

All entities registered in India like banks, financial institutions, Primary Dealers, firms, companies, corporate bodies, partnership firms, institutions, mutual funds, Foreign Institutional Investors, State Governments, Provident Funds, trusts, research organisations, Nepal Rashtra bank and even individuals are eligible to bid and purchase Treasury bills.

(d) Repayment

The treasury bills are repaid at par on the expiry of their tenure at the office of the Reserve Bank of India.

(e) Availability

All the treasury bills are highly liquid instruments available both in the primary and secondary market.

(f) Day Count

For treasury bills the day count is taken as 365 days for a year.

(g) Yield Calculation

The yield of a Treasury Bill is calculated as per the following formula:

$$Y = \frac{(100 - P) \times 365 \times 100}{P \times D}$$

Wherein Y = Discounted yield

P = Price

D = Days to maturity

Example

A cooperative bank wishes to buy 91 days Treasury Bill on Oct. 12, 2014 which is maturing on Dec. 6, 2014. The rate quoted by seller is ₹ 99.1489 per ₹ 100 face values. The YTM can be calculated as following:

The days to maturity of Treasury bill are 55 (October – 20 days, November – 30 days and December – 5 days)

$$YTM = (100 - 99.1489) \times 365 \times 100 / (99.1489 \times 55) = 5.70\%$$

Similarly if the YTM is quoted by the seller, price can be calculated by putting the price in above formula.

Primary Market

In the primary market, treasury bills are issued by auction technique.

Salient Features of the Auction Technique:

- (a) The auction of treasury bills is done only at Reserve Bank of India, Mumbai.
- (b) Bids are to be submitted on Negotiated Dealing System (NDS) by 2:30 PM on Wednesday. If Wednesday happens to be a holiday then bids are to be submitted on previous day (Tuesday).
- (c) Bids are submitted in terms of price per ₹ 100. For example, a bid for 91-days Treasury bill auction could be for ₹ 97.50 for per unit of T-bill of face value of ₹ 100.
- (d) Auction committee of Reserve Bank of India decides the cut-off price and results are announced on the same day.
- (e) Bids above the cut-off price receive full allotment; bids at cut-off price may receive full or partial allotment and bids below the cut-off price are rejected.

Secondary Market

The participants can also trade T-bills held from primary market in the secondary market established for the purpose. The major advantages of dealing in treasury bill secondary market are: Market related yields, ideal matching for funds management particularly for short-term tenors of less than 15 days, Transparency in operations as the transactions would be put through Reserve Bank of India's SGL or Client's Gilt account only, two way quotes offered by primary dealers for purchase and sale of treasury bills and certainty in terms of availability, entry and exit.

TYPES OF AUCTION

There are two types of auction for treasury bills:

- **Multiple Price Based or French Auction:** Under this method, all bids equal to or above the cut-off price are accepted. However, the bidder has to obtain the treasury bills at the price quoted by him. This method is followed in the case of 364 days treasury bills and is valid only for competitive bidders.
- **Uniform Price Based or Dutch Auction:** Under this system, all the bids equal to or above the cut-off price are accepted at the cut-off level. However, unlike the Multiple Price based method, the bidder obtains the treasury bills at the cut-off price and not the price quoted by him. This method is applicable in the case of 91 days treasury bills only. The system of Dutch auction has been done away with by the RBI w.e.f 08.12.2002 for the 91 days Treasury Bill.

What is Dutch auction?

When all the bids accepted at the cut off level it is known as Dutch Auction.

What is French Auction?

When all the bids accepted are equal to or above the cut off price it is known as French Auction.

CERTIFICATES OF DEPOSITS

Certificate of Deposits (CDs) is a negotiable money market instrument and issued in dematerialised form or as Usance Promissory Note, against funds deposited at a bank or other eligible financial institution for a specified time period. Guidelines for issue of CDs are presently governed by various directives issued by the Reserve Bank of India, as amended from time to time.

ELIGIBILITY

CDs can be issued by:

- (i) scheduled commercial banks excluding Regional Rural Banks (RRBs) and Local Area Banks (LABs); and
- (ii) selected all-India Financial Institutions that have been permitted by RBI to raise short-term resources within the umbrella limit fixed by RBI.

AGGREGATE AMOUNT

The amount of CDs allowed to be issued by:

- (i) **Banks:** varying according to the requirements keeping in limits the CRR and SLR requirements as stipulated by RBI.
- (ii) **Financial Institutions:** may issue CDs within the overall umbrella limit fixed by RBI. As per the prevailing guidelines issued by RBI, an FI can issue CDs together with other instruments viz., term money, term deposits, commercial papers and inter corporate deposits, not exceeding 100 per cent of its net owned funds, as per the latest audited balance sheet.

MINIMUM SIZE OF ISSUE AND DENOMINATIONS

Minimum amount of a CD should be ₹1 lakh i.e., the minimum deposit that could be accepted from a single subscriber should not be less than ₹1 lakh and in the multiples of ₹ 1 lakh thereafter. CDs can be issued to individuals, corporations, companies, trusts, funds, associations, etc. Non-Resident Indians (NRIs) may also subscribe to CDs, but only on non-repatriable basis which should be clearly stated in the Certificate. Such CDs cannot be endorsed to another NRI in the secondary market.

MATURITY

The maturity period of CDs issued by banks should not be less than 7 days and not more than one year from the date of issue. The FIs can issue CDs for a period not less than 1 year and not exceeding 3 years from the date of issue.

DISCOUNT/COUPON RATE

CDs may be issued at a discount on face value. Banks/FIs are allowed to issue CDs on the basis of floating rate provided the methodology of compiling the floating rate is objective transparent and market based. The issuing bank/FI is free to determine the discount/coupon rate. The interest rate on floating rate CDs would have to be reset periodically in accordance with a pre-determined formula that indicates the spread over a transparent benchmark.

RESERVE REQUIREMENTS

Banks have to maintain the appropriate reserve requirements, i.e., cash reserve ratio (CRR) and statutory liquidity ratio (SLR), on the issue price of the CDs.

TRANSFERABILITY

- Physical CDs are freely transferable by endorsement and delivery.
- Demat CDs can be transferred as per the procedure applicable to other demat securities.
- There is no lock-in period for the CDs.

- Banks/FIs cannot grant loans against CDs.
- Furthermore, they cannot buy-back their own CDs before maturity.

TRADES IN CDs

All OTC trades in CDs shall be reported within 15 minutes of the trade on the reporting platform Clearcorp Dealing Systems (India) Ltd. (CDSIL).

FORMAT OF CDs

Banks/FIs should issue CDs only in the dematerialised form. However, according to the Depositories Act, 1996, investors have the option to seek certificate in physical form. Accordingly, if the investor insists on physical certificate, the bank/FI may inform to Chief General Manager, Financial Markets Regulation Department, Reserve Bank of India about such instances separately. Further, **issuance of CD will attract stamp duty**. There will be no grace period for repayment of CDs. If the maturity date happens to be holiday, the issuing bank should make payment on the immediate preceding working day. Banks/FIs may, therefore, so fix the period of deposit that the maturity date does not coincide with a holiday to avoid loss of discount / interest rate.

SECURITY ASPECT

Since physical CDs are freely transferable by endorsement and delivery, it will be necessary for banks to see that the certificates are printed on good quality security paper and necessary precautions are taken to guard against tempering with the document. They should be signed by two or more authorized signatories.

PAYMENT OF CERTIFICATE

Since CDs are transferable, the physical certificate may be presented for payment by the last holder. The question of liability on account of any defect in the chain of endorsements may arise. It is, therefore, desirable that banks take necessary precautions and make payment only by a crossed cheque. Those who deal in these CDs may also be suitably cautioned. The holders of dematted CDs will approach their respective depository participants (DPs) and have to give transfer/delivery instructions to transfer the demat security represented by the specific ISIN to the 'CD Redemption Account' maintained by the issuer. The holder should also communicate to the issuer by a letter/fax enclosing the copy of the delivery instruction it had given to its DP and intimate the place at which the payment is requested to facilitate prompt payment. Upon receipt of the demat credit of CDs in the "CD Redemption Account", the issuer, on maturity date, would arrange to repay to holder/transferor by way of Banker's cheque/high value cheque, etc.

ISSUE OF DUPLICATE CERTIFICATES

In case of the loss of physical CD certificates, duplicate certificates can be issued after compliance of the following conditions:

- (a) A notice is required to be given in at least one local newspaper;
- (b) Lapse of a reasonable period (say 15 days) from the date of the notice in the newspaper; and
- (c) Execution of an indemnity bond by the investor to the satisfaction of the issuer of CDs.

The duplicate certificate should only be issued in physical form. No fresh stamping is required as a duplicate certificate is issued against the original lost CD. The duplicate CD should clearly state that the CD is a Duplicate one stating the original value date, due date, and the date of issue (as "Duplicate issued on _____").

ACCOUNTING

Banks/FIs may account the issue price under the Head "CDs issued" and show it under deposits. Accounting entries towards discount will be made as in the case of "cash certificates". Banks/FIs should maintain a register of CDs issued with complete particulars.

INTER-CORPORATE DEPOSITS

Apart from CDs, corporates also have access to another market called the Inter Corporate Deposits (ICD) market. An ICD is an unsecured loan extended by one corporate to another. Existing mainly as a refuge for low rated corporates, this market allows corporates with surplus funds to lend to other corporates facing shortage of funds. Another aspect of this market is that the better-rated corporates can borrow from the banking system and lend in this market to make speculative profits. As the cost of funds for a corporate is much higher than that of a bank, thus, the rates in this market are higher than those in the other markets. ICDs are unsecured, and hence the risk inherent is high. The ICD market is an unorganised market with very less information available publicly about transaction details.

COMMERCIAL BILLS

Commercial bills are basically negotiable instruments accepted by buyers for goods or services obtained by them on credit. Such bills being bills of exchange can be kept upto the due maturity date and encashed by the seller or may be endorsed to a third party in payment of dues owing to the latter. The most common practice is that the seller who gets the accepted bills of exchange discounts it with the Bank or financial institution or a bill discounting house and collects the money (less the interest charged for the discounting).

The volume of bills both inland and foreign, which are discounted accounted, forms a substantial part of the total scheduled commercial bank credit. Over the years this is coming down. The Reserve Bank has been attempting to develop a market for commercial bills. The bill market scheme was introduced in 1942 and a new scheme called Bill Rediscount Scheme with several new features was introduced in November, 1970. Under the latter scheme the RBI rediscount bills at the bank rates or at rates specified by it at its discretion. Since the rediscounting facility has been made restrictive, it is generally available on a discretionary basis.

The difficulties which stand in the way of bill market development are, the incidence of stamp duty, shortage of stamp paper, reluctance of buyers to accept bills, predominance of cash credit system of lending and the administrative work involved in handling documents of title to goods. To be freely negotiable and marketable, the bills should be first class bills i.e. those accepted by companies having good reputation. Alternatively, the bills accepted by companies should be co-accepted by banks as a kind of guarantee. In the absence of these criteria, bill market has not developed in India as the volume of first class bills is very small.

COMMERCIAL PAPER

Commercial Paper (CP) is an unsecured money market instrument issued in the form of a promissory note. CP, as a privately placed instrument, was introduced in India in 1990 with a view to enable highly rated corporate borrowers to diversify their sources of short-term borrowings and to provide an additional instrument to investors. Subsequently, primary dealers (PDs), and all-India financial institutions were also permitted to issue CP to enable them to meet their short-term funding requirements for their operations. The Guidelines for issue of CP are presently governed by various directives issued by the Reserve Bank of India, as amended from time to time.

The guidelines for issue of CP are given below:

Eligible issuers of CP

Companies, PDs and financial institutions (FIs) are permitted to raise short-term resources under the umbrella limit fixed by the Reserve Bank of India (RBI) are eligible to issue CP.

A company would be eligible to issue CP provided:

- (a) the tangible net worth of the company, as per the latest audited balance sheet, is not less than ₹ 4 crore;
- (b) the company has been sanctioned working capital limit by bank/s or FIs; and

- (c) the borrowal account of the company is classified as a Standard Asset by the financing bank/institution.

Rating Requirements

All eligible participants shall obtain credit rating for issuance of CP from any one of the SEBI registered Credit Rating Agencies.

The minimum credit rating shall be 'A3' [as per rating symbol and definition prescribed by Securities and Exchange Board of India (SEBI)].

Maturity

CP can be issued for maturities between a minimum of 7 days and a maximum of up to one year from the date of issue. The maturity date of the CP should not go beyond the date up to which the credit rating of the issuer is valid.

Denominations

CP can be issued in denominations of ₹ 5 lakh and multiples thereof. The amount invested by a single investor should not be less than ₹ 5 lakh (face value).

Limits and the Amount of Issue of CP

The aggregate amount of CP from an issuer shall be within the limit as approved by its Board of Directors or the quantum indicated by the CRA for the specified rating, whichever is lower. Banks and FIs will, however, have the flexibility to fix working capital limits, duly taking into account the resource pattern of company's financing, including CPs.

An FI can issue CP shall be within the overall umbrella limit prescribed in the Master Circular on Resource Raising Norms for FIs, issued by Reserve Bank of India, Department of Banking Regulation as prescribed and updated from time-to-time.

The total amount of CP proposed to be issued should be raised within a period of two weeks from the date on which the issuer opens the issue for subscription.

Issuing and Paying Agent (IPA)

Only a scheduled bank can act as an IPA for issuance of CP.

Investment in CP

CP may be issued to individuals, banking companies, other corporate bodies (registered or incorporated in India) and unincorporated bodies, Non-Resident Indians and Foreign Institutional Investors (FIIs). However, investment by FIIs would be within the limits set for them by SEBI and compliance with the provisions of the FEMA 1999, the Foreign Exchange (Deposit) Regulations, 2000 and Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2000, as amended from time to time.

Trading in CP

All OTC trades in CP shall be reported within 15 minutes of the trade to the reporting platform of Clearcorp Dealing Systems (India) Ltd. (CDSIL)

Mode of Issuance

CP can be issued either in the form of a promissory note and held in physical form or in a dematerialised form through any of the depositories approved by and registered with SEBI. Provided all RBI regulated entities can deal in and hold CP only in dematerialised form through such depositories. CP will be issued at a discount to

face value as may be determined by the issuer. No issuer shall have the issue of CP underwritten or co-accepted.

Preference for Dematerialisation

While option is available to both issuers and subscribers to issue/hold CP in dematerialised or physical form, issuers and subscribers are encouraged to opt for dematerialised form of issue/holding. However, banks, FIs and PDs are required to make fresh investments and hold CP only in dematerialised form.

Payment of CP

The initial investor in CP shall pay the discounted value of the CP by means of a crossed account payee cheque to the account of the issuer through IPA. On maturity of CP, when CP is held in physical form, the holder of CP shall present the instrument for payment to the issuer through the IPA. However, when CP is held in demat form, the holder of CP will have to get it redeemed through the depository and receive payment from the IPA.

Procedure for Issuance

Every issuer must appoint an IPA for issuance of CP. The issuer should disclose to the potential investors, its financial position as per the standard market practice. After the exchange of deal confirmation between the investor and the issuer, issuing company shall issue physical certificates to the investor or arrange for crediting the CP to the investor's account with a depository. Investors shall be given a copy of IPA certificate to the effect that the issuer has a valid agreement with the IPA and documents are in order.

Role and Responsibilities

The role and responsibilities of issuer, IPA and CRA are set out below:

(a) Issuer

With the simplification in the procedures for issuance of CP, issuers would now have greater flexibility. However, they have to ensure that the guidelines and procedures laid down for CP issuance are strictly adhered to.

(b) Issuing and Paying Agent (IPA)

- (i) The IPA would ensure that the issuer has the minimum credit rating as stipulated by RBI and the amount mobilised through issuance of CP is within the quantum indicated by CRA for the specified rating or as approved by its Board of Directors, whichever is lower.
- (ii) The IPA has to verify all the documents submitted by the issuer, viz., copy of board resolution, signatures of authorised executants (when CP is issued in physical form) and issue a certificate to this effect.
- (iii) Certified copies of original documents, verified by the IPA, should be held in the custody of IPA.
- (iv) All scheduled banks, acting as the IPAs should submit the data pertaining to CP issuances on the Online Returns Filing System (ORFS) module of the RBI within two days from the date of issuance of CP.
- (v) The IPA shall certify that it has a valid agreement with the issuer.

(c) CRA

- (i) The CRA shall abide by the Code of Conduct prescribed by the SEBI for CRAs for undertaking rating of capital market instruments shall be applicable to CRAs for rating CPs.
- (ii) The CRAs would henceforth have the discretion to determine the validity period of the rating depending

upon its perception about the strength of the issuer. Accordingly, they shall, at the time of rating, clearly indicate the date when the rating is due for review.

- (iii) The CRAs would have to closely monitor the rating assigned to issuers vis-à-vis their track record at regular intervals and would be required to make their revision in the ratings public through their publications and website

FACTORING

Factoring is a financial transaction where an entity sells its receivables to a third party called a 'factor', at discounted prices. Factoring is a financial option for the management of receivables. In simple definition it is the conversion of credit sales into cash. In factoring, a financial institution (factor) buys the accounts receivable of a company (Client) and pays up to 80%(rarely up to 90%) of the amount immediately on formation of agreement. Factoring company pays the remaining amount (Balance 20%-finance cost-operating cost) to the client when the customer pays the debt. Collection of debt from the customer is done either by the factor or the client depending upon the type of factoring. The account receivable in factoring can either be for a product or service. Examples : factoring against goods purchased, factoring for construction services (usually for government contracts where the government body is capable of paying back the debt in the stipulated period of factoring. Contractors submit invoices to get cash instantly), factoring against medical insurance etc.

PARTIES IN FACTORING

The factoring transaction involves three parties:

- The Seller, who has produced the goods/services and raised the invoice.
- The Buyer, the consumer of goods/services and the party to pay.
- The Factor, the financial institution that advances the portion of funds to the seller.

FACTORING PROCESS

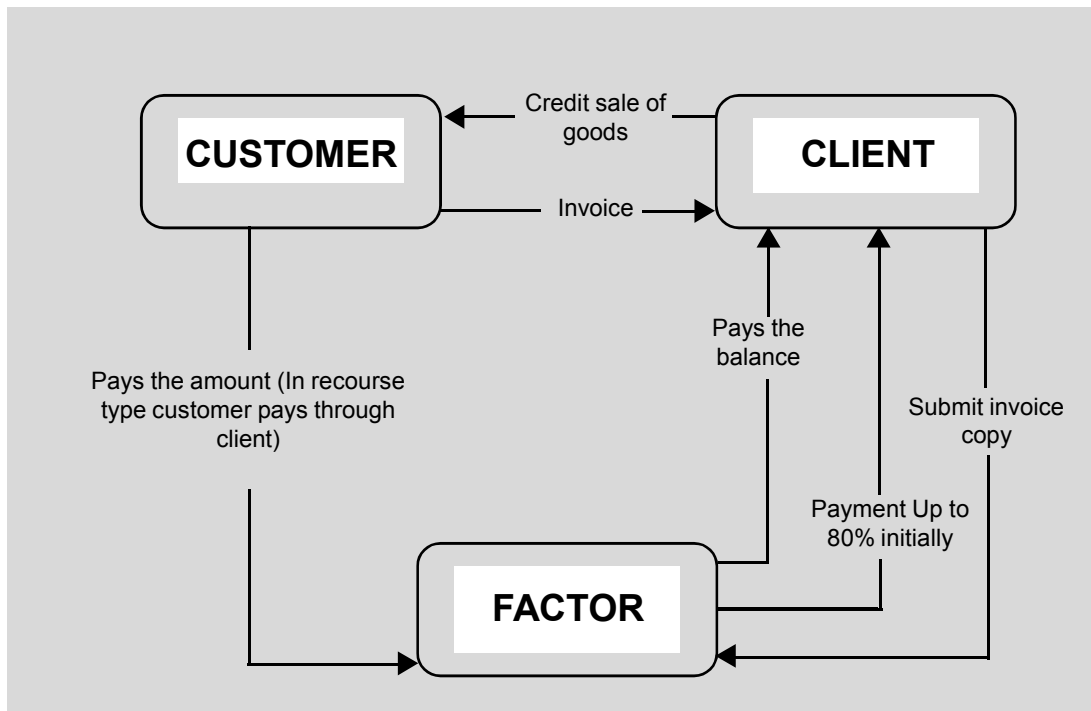
The steps involved in factoring are listed below:

- The seller interacts with the funding specialist/broker and explains the funding needs.
- The broker prepares a preliminary client profile form and submits to the appropriate funder for consideration.
- Once both parties agree that factoring is possible, the broker puts the seller in direct contact with the funder to ask/answer any additional questions and to negotiate a customized factoring agreement, which will meet the needs of all concerned.
- At this point, the seller may be asked to remit a fee with formal application to cover the legal research costs, which will be incurred during "due diligence". This is the process by which the buyer's credit worthiness is evaluated through background checks, using national database services.
- During the next several days, the funder completes the "due diligence" process on the seller, further verifies invoices and acknowledges any liens, UCC filings, judgments or other recorded encumbrances on the seller's accounts receivables.
- The seller is advised of the facility and is asked to advise the buyers of the Factor by letter and submit an acknowledged copy of the same to the Factor for records.
- A detailed sanction letter is given to the seller and their acceptance on the same taken, with the required signatories. (Authorized signatories would be mentioned in the "Signing Authorities" section of the Proposal presented by seller).

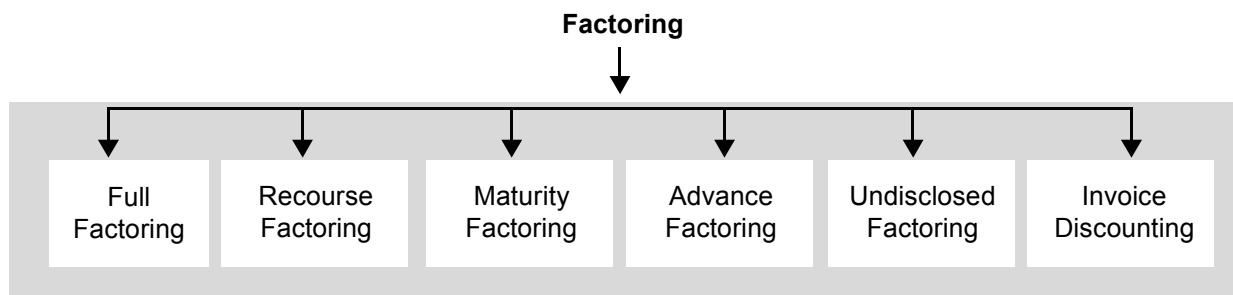
- Sanction terms must contain the following.
 - All facilities covered under the sanction.
 - The period for which the sanction is valid
 - When the facility comes into effect e.g. (if facility is dated 1/12/13, it can state that invoices raised from or after 15/12/13 only would be Factored).
 - Who the authorized signatories are for signing invoices for factoring.
 - The limits.
 - The seller has to advise the buyer of the Factoring agreement.
 - Copy of such advice acknowledged by the buyer should be submitted to the Factor. Buyer's consent is not required to decide on the Factor.
- The discounting rates, charges fixed.
- In case of discounts given by the seller to the buyer, which value would be financed by the factor (since the factored amount should never exceed the amount actually payable by buyer).
- Usually within 7 to 10 days of the initial contact with the factor, agreements are signed, customers are notified, UCC forms filed and the first advance is forwarded to the company. This advance can vary between 70 - 80% of the face value of the invoices being factored. In the construction industry, the advances may be in the range of 60 - 70%. The remaining amount is called the "reserve" which is held by the factor until the invoices are paid. The factor then deducts his fee and returns the remaining funds to the seller.
- The seller performs services or delivers products, thus creating an invoice.
- The seller sends or faxes a copy of the invoice directly to the factor.
- The funder verifies the invoice and the advance is sent to the seller as per the agreement with the factor. In certain cases, the funder wires the funds to the seller's account for an additional fee.
- The buyer pays the factor. The factor then returns any remaining reserve, minus the fee, which has been predetermined in the negotiated agreement.

ADVANTAGES FOR THE SELLER

- Seller gets funds immediately after the sale is effected and on presentation of accepted sales invoices and Promissory notes.
- Major part of paper work and correspondence is taken care of by the factor.
- Follow-up, for recovery of funds, is done mainly by the factor.
- Interest rates are not as high as normal discounting.
- Increased cash flow to meet payroll.
- Immediate funding arrangements.
- No additional debt is incurred on balance sheet.
- Other assets are not encumbered.
- Approval is not based on seller's credit rating.



TYPES OF FACTORING



Non-Recourse or Full factoring

Under this type of factoring the bank takes all the risk and bear all the loss in case of debts becoming bad debts.

Recourse Factoring

Under this type of factoring the bank purchases the receivables on the condition that any loss arising out or bad debts will be borne by the company which has taken factoring.

Maturity Factoring

Under this type of factoring bank does not give any advance to the company rather bank collects it from customers and pays to the company either on the date of collection from the customers or on a guaranteed payment date.

Advance Factoring

Under advance factoring arrangement the factor provides an advance against the uncollected and non-due receivables to the firm.

Undisclosed Factoring

Under this type of factoring, the customer is not informed of the factoring arrangement. The firm may collect dues from the customer on its own or instruct to make remit once at some other address.

Invoice Discounting

Under this type of factoring the bank provide an advance to the company against the account receivables and in turn charges interest rate from the company for the payment which bank has given to the company.

BILLS REDISCOUNTING

Bill rediscounting means the rediscounting of trade bills, which have already been purchased by/discounted with the bank by the customers. These trade bills arise out of supply of goods/services. Bill rediscounting is a money market instrument where the bank buys the bill (i.e. Bill of Exchange or Promissory Note) before it is due and credits the value of the bill after a discount charge to the customer's account. Now, the bank which has discounted the bill may require getting it 'rediscounted' with some other bank to get the fund.

Features

- The banks normally rediscount the bills that have already been discounted with them or raise usance promissory notes in convenient lots and maturities and rediscount them.
- Rediscount of bills should be for a minimum period of 15 days and for a maximum period of 90 days.
- Discount is calculated on Actual/365 days basis.
- The amount payable to the borrower is the principal amount less the discount/interest.
- While discounting a bill, the amount of discount is to be deducted at the time the bill is issued.
- The discount is rounded off to the nearest rupee.
- On maturity the borrower would repay the principal amount.

LESSON ROUND UP

- Money market is a very important segment of the Indian financial system. It is the market for dealing in monetary assets of short-term nature.
- There are a large number of participants in the money market: commercial banks, mutual funds, investment institutions, financial institutions and the Regulatory Authority.
- The money market possesses different operational features as compared to capital market. It deals with raising and deployment of funds for short duration while the capital market deals with long-term funding.
- The money market operates as a wholesale market and has a number of inter-related sub-markets such as the call market, the bill market, the treasury bill market, the commercial paper market, the certificate of deposits market etc.
- Money market instruments mainly include Government securities, securities issued by banking sector and securities issued by private sector.
- Treasury Bills are money market instruments to finance the short term requirements of the Government of India.
- Certificates of Deposits (CDs) is a negotiable money market instrument and is issued in dematerialised form or as a Usance Promissory Note, against funds deposited at a bank or other eligible financial institution for a specified time period.

- Commercial bills are basically negotiable instruments accepted by buyers for goods or services obtained by them on credit.
- Commercial Paper (CP) is an unsecured money market instrument issued in the form of a promissory note. CP, as a privately placed instrument, was introduced in India in 1990 with a view to enabling highly rated corporate borrowers to diversify their sources of short-term borrowings and to provide an additional instrument to investors.
- Factoring is a Financial transaction where an entity sells its receivables to a third parties called a factor, at discounted prices.

GLOSSARY

CRR	Cash reserve ratio is the cash parked by the banks in their specified current account maintained with RBI.
DFHI	The Discount and Finance House of India Limited(DFHI) has been set up by the Reserve bank of India jointly with public sector banks and all India Financial Institutions to deal in short term money market instruments.
FIMMDA	The Fixed Income Money Market and Derivatives Association of India (FIMMDA), an association of Scheduled Commercial Banks, Public Financial Institutions, Primary Dealers and Insurance Companies was incorporated as a Company under section 8 of the Companies Act, 2013. FIMMDA is a voluntary market body for the bond, money and derivatives markets.
Negotiated Dealing System (NDS)	An electronic trading platform, operated by the Reserve Bank of India, used to facilitate the exchange of government securities and other money market instruments. The negotiated dealing system will also be responsible for hosting new issues of government securities.
Online Returns Filing System (ORFS)	It is a single window return submission system for submission of certain important returns by Commercial Bank to the Reserve Bank of India
Repo rate	The rate at which the RBI lends money to commercial banks is called repo rate. It is an instrument of monetary policy. Whenever banks have any shortage of funds they can borrow from the RBI.
SLR	Statutory liquidity ratio is in the form of cash (book value), gold (current market value) and balances in unencumbered approved securities.
Yield to maturity (YTM)	The Yield to maturity (YTM) is the yield promised to the bondholder on the assumption that the bond will be held to maturity and coupon payments will be reinvested at the YTM. It is a measure of the return of the bond.

SELF TEST QUESTIONS

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation.)

1. "Money market is very important segment of Indian Financial System". Comment and discuss various features of money market.
2. State how yield of Treasury Bill is calculated.
3. Briefly discuss the guidelines for issue of commercial paper.

4. Discuss the role and responsibilities of issuer, issuing and paying agent and credit rating agency in issuance of commercial paper.
5. Discuss various types of factoring.
6. What is Bill rediscounting?

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Lesson 7

Mutual Funds

LESSON OUTLINE

- Introduction
- An Overview of Trends in Mutual Funds
- Advantages of Mutual Funds
- Schemes of according to maturity period
- Investment Strategies
- Offer Document of Mutual Fund Scheme
- Additional mode of payment through Applications Supported by Blocked Amount in mutual funds
- Risks Involved in Mutual Funds
- Calculation of Net Asset Value
- Mutual Fund Costs
- Transaction charges
- Roll Over of a Scheme
- Switch Over one Scheme to Another
- Annualised Returns
- Asset Management Company
- Restriction on Redemption in Mutual Funds
- SEBI (Mutual Fund) Regulations, 1996
- Code of Conduct for Mutual Funds
- General and specific due diligence by trustees
- Independent Director's Responsibilities
- Procedure for launching of schemes
- Advertisement Code for Mutual Funds
- In principle approval from RSEs
- Listing of close ended scheme
- Repurchase of close ended scheme
- Offering period
- Allotment of units and refund of money
- Transfer of units
- Guaranteed Returns
- Capital protection oriented scheme
- Infrastructure Debt fund Scheme
- Gold Exchange Traded Funds
- Real Estate Mutual Fund Schemes
- Compliance under SEBI (Listing Obligation and Disclosure Requirements) Regulations, 2015
- LESSON ROUND-UP
- GLOSSARY
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

Different investment avenues are available to investors, one of them being Mutual Fund. Mutual fund is a mechanism for pooling the resources by issuing units to the investors and investing funds in securities in accordance with objectives as disclosed in offer document.

Mutual funds offer good investment opportunities to the investors. Like all investments, they also carry certain risks. The investors should compare the risks and expected yields after adjustment of tax on various instruments while taking investment decisions.

SEBI formulates policies and regulates the mutual funds to protect the interest of the investors. SEBI notified regulations for the mutual funds in 1993. Thereafter, mutual funds sponsored by private sector entities were allowed to enter the capital market. The regulations were fully revised in 1996 and have been amended thereafter from time to time.

Keeping the above in view this lesson is designed to enable the students to understand the trend of mutual funds in India over a period of time. Various schemes of mutual funds, advantages and risk involved in Mutual Fund and SEBI regulations and compliance under SEBI (Listing Obligation and Disclosure Requirements) Regulations, 2015 pertaining the mutual fund operating in India etc.

INTRODUCTION

Mutual fund is a mechanism for pooling the resources by issuing units to the investors and investing funds in securities in accordance with objectives as disclosed in offer document. Investments in securities are spread across a wide cross-section of industries and sectors and thus the risk is reduced. Diversification reduces the risk because all stocks may not move in the same direction in the same proportion at the same time. Mutual fund issues units to the investors in accordance with quantum of money invested by them. Investors of mutual funds are known as unitholders. The profits or losses are shared by the investors in proportion to their investments. The mutual funds normally come out with a number of schemes with different investment objectives which are launched from time to time. A mutual fund is required to be registered with SEBI before it can collect funds from the public.

The small investors who generally lack expertise to invest on their own in the securities market have reinforced the saying “Put not your trust in money, put your money in trust”. They prefer some kind of collective investment vehicle like, MFs, which pool their marginal resources, invest in securities and distribute the returns therefrom among them on cooperative principles. The investors benefit in terms of reduced risk and higher returns arising from professional expertise of fund managers employed by the MFs. This approach was conceived in the USA in the 1930s. In developed financial markets, MFs have almost overtaken bank deposits and total assets of insurance funds.

Experiment with MFs in India began in 1964 with the establishment of Unit Trust of India (UTI). UTI lost its monopoly status in 1987 with the entry of other public sector MFs promoted by public sector banks and insurance companies. The industry was opened to private sector, including foreign institutions, in 1993 giving Indian investors a broader choice and increasing competition to public sector funds.

AN OVERVIEW OF TRENDS IN MUTUAL FUNDS

As in mature markets, mutual funds in emerging markets have been among the fastest growing institutional investors. One key difference between mutual funds of mature and emerging markets has been the relative importance of bond and equity funds are often much larger than those of bond funds, (particularly in Japan, the United Kingdom, the United States). In contrast, emerging market bond funds in a number of countries have larger assets under management than do equity funds particularly in Brazil, Mexico, Korea and Taiwan. In part, this reflects the difference in the relative development of the local markets in mature and emerging markets. This difference reflects a search for higher yield on the part of retail investors. As the nominal interest rates have declined in many emerging countries since the late 1990s, retail investors have seen an extended decline in the interest rate of traditional savings instruments. To obtain higher yields, retail investors should subscribe to bond funds with investment in longer term government and corporate bonds.

Household savings play an important role in domestic capital formation. Only a small part of the household savings in India is channelised to the capital market. Attracting more households to the capital market requires efficient intermediation. The mutual funds have emerged as one of the important class of financial intermediaries which cater to the needs of retail investors. As a traditional investment vehicle, the mutual funds pool resources from the households and allocate them to various investment opportunities.

ADVANTAGES OF MUTUAL FUNDS

The advantages of investing in a mutual fund are:

1. **Professional Management:** Investors avail the services of experienced and skilled professionals who are backed by a dedicated investment research team which analyses the performance and prospects of companies and selects suitable investments to achieve the objectives of the scheme.

2. **Diversification:** Mutual funds invest in a number of companies across a broad cross-section of industries and sectors. This diversification reduces the risk because seldom do all stocks decline at the same time and in the same proportion. Investors achieve this diversification through a Mutual Fund with far less money than one can do on his own.
3. **Convenient Administration:** Investing in a mutual fund reduces paper work and helps investors to avoid many problems such as bad deliveries, delayed payments and unnecessary follow up with brokers and companies. Mutual funds save investors time and make investing easy and convenient.
4. **Return Potential:** Over a medium to long term, Mutual funds have the potential to provide a higher return as they invest in a diversified basket of selected securities.
5. **Low Costs:** Mutual funds are a relatively less expensive way to invest compared to directly investing in the capital markets because the benefits of scale in brokerage, custodial and other fees translate into lower costs for investors.
6. **Liquidity:** In open ended schemes, investors can get their money back promptly at net asset value related prices from the mutual fund itself. With close ended schemes, investors can sell their units on a stock exchange at the prevailing market price or avail of the facility of direct repurchase at net asset value (NAV) related prices which some close ended and interval schemes offer periodically or offer it for redemption to the fund on the date of maturity.
7. **Transparency:** Investors get regular information on the value of their investment in addition to disclosure on the specific investments made by scheme, the proportion invested in each class of assets and the fund manager's investment strategy and outlook.

SCHEMES ACCORDING TO MATURITY PERIOD

The MFs in India offer a wide array of schemes that cater to different needs suitable to any age, financial position, risk tolerance and return expectations. These include: open-ended schemes, which provide easy liquidity; close-ended schemes with a stipulated maturity period; growth schemes, which provide capital appreciation over medium to long term; income schemes, which provide regular and steady income to investors; balanced schemes, which provide both growth and income by periodically distributing a part of income and capital gains they earn; money market schemes; which provide easy liquidity, preservation of capital and moderate income; and tax saving schemes, which offer tax rebates to investors under tax laws as prescribed from time to time.

(i) Open ended mutual funds: An open ended mutual funds is a fund with a non-fixed number of outstanding shares/units, that stands ready at any time to redeem them on demand. The fund itself buys back the shares surrendered and is ready to sell new shares. Generally the transaction takes place at the net asset value which is calculated on a periodical basis. The net asset value (Net Asset Value per share-value of the fund's is total net assets after liabilities divided by the total number of shares outstanding on a given day) of the mutual funds rises or falls as a result of the performance of securities in the portfolio and the stock exchanges. The key feature of open ended scheme is liquidity.

(ii) Close ended mutual funds: It is the fund where mutual fund management sells a limited number of shares and does not stand ready to redeem them. Generally the transaction takes place at the net asset value which is calculated on a weekly basis. The shares of such mutual funds are traded in the secondary markets. The requirement for listing is laid down to grant liquidity to the investors who have invested with the mutual fund. Therefore, close ended funds are more like equity shares. The main differences between close ended and open ended funds are :

CLOSE ENDED SCHEMES	OPEN ENDED SCHEMES
1. Fixed corpus: no new units can be offered beyond the limit.	1. Variable corpus due to on going purchase and redemption.
2. Listed on the stock exchange for buying and selling.	2. No listing on exchange transactions done directly with the fund.
3. Two values available namely NAV and the Market Trading Price.	3. Only one price namely NAV.
4. Mostly liquid.	4. Highly Liquid.

SCHEMES ACCORDING TO INVESTMENT OBJECTIVE

Besides these, there are other types of mutual funds also to meet the investment needs of several groups of investors. Some of them include the following:

- (a) **Income Oriented Schemes:** The fund primarily offer fixed income to investors. Naturally enough, the main securities in which investments are made by such funds are the fixed income yielding ones like bonds, corporate debentures, Government securities and money market instruments, etc.
- (b) **Growth Oriented Schemes:** These funds offer growth potentialities associated with investment in capital market namely: (i) high source of income by way of dividend and (ii) rapid capital appreciation, both from holding of good quality scrips. These funds, with a view to satisfying the growth needs of investors, primarily concentrate on the low risk and high yielding spectrum of equity scrips of the corporate sector.
- (c) **Hybrid Schemes:** These funds cater to both the investment needs of the prospective investors - namely fixed income as well as growth orientation. Therefore, investment targets of these mutual funds are judicious mix of both the fixed income securities like bonds and debentures and also sound equity scrips. In fact, these funds utilise the concept of balanced investment management. These funds are, thus, also known as "balanced funds".
- (d) **High Growth Schemes:** As the nomenclature depicts, these funds primarily invest in high risk and high return volatile securities in the market and induce the investors with a high degree of capital appreciation.
- (e) **Capital Protection Oriented Scheme:** It is a scheme which protects the capital invested in the mutual fund through suitable orientation of its portfolio structure.
- (f) **Tax Saving Schemes:** These schemes offer tax rebates to the investors under tax laws as prescribed from time to time. This is made possible because the Government offers tax incentive for investment in specified avenues. For example, Equity Linked Saving Schemes (ELSS) and pensions schemes.
- (g) **Special Schemes:** This category includes index schemes that attempt to replicate the performance of particular index such as the BSE, Sensex or the NSE-50 or industry specific schemes (which invest in specific industries) or sectoral schemes (which invest exclusively in segment such as 'A' Group or initial public offering). Index fund schemes are ideal for investors who are satisfied with a return approximately equal to that of an index. Sectoral fund schemes are ideal for investors who have already decided to invest in particular sector or segment.
- (h) **Real Estate Funds:** These are close ended mutual funds which invest predominantly in real estate and properties.
- (i) **Off-shore Funds:** Such funds invest in securities of foreign companies with RBI permission.

- (j) **Leverage Funds:** Such funds, also known as borrowed funds, increase the size and value of portfolio and offer benefits to members from out of the excess of gains over cost of borrowed funds. They tend to indulge in speculative trading and risky investments.
- (k) **Hedge Funds:** They employ their funds for speculative trading, i.e. for buying shares whose prices are likely to rise and for selling shares whose prices are likely to fall.
- (l) **Fund of Funds:** They invest only in units of other mutual funds. Such funds do not operate at present in India.
- (m) **New Direction Funds:** They invest in companies engaged in scientific and technological research such as birth control, anti-pollution, oceanography etc.
- (n) **Exchange Trade Funds (ETFs)** are a new variety of mutual funds that first introduced in 1993. ETFs are sometimes described as mere “tax efficient” than traditional equity mutual funds, since in recent years, some large ETFs have made smaller distribution of realized and taxable capital gains than most mutual funds.
- (o) **Money Market Mutual Funds:** These funds invest in short- term debt securities in the money market like certificates of deposits, commercial papers, government treasury bills etc. Owing to their large size, the funds normally get a higher yield on such short term investments than an individual investor.
- (p) **Infrastructure Debt Fund :** They invest primarily in the debt securities or securitized debt investment of infrastructure companies.

INVESTMENT STRATEGIES

Bottom up Investing: This is an investment strategy which considers the fundamental factors driving individual stock performance before considering the economic prospectus which affect the industry and within which the company operates.

Top down Investing: This is an investment strategy which first takes a view on the economy and then looks at the industry scenario to assess the potential performance of a company. This is opposite to Bottom up Technique.

Equity funds are considered aggressive in so far as higher capitalisation is sought. Investors should have a long term orientation, since companies shares give fluctuating dividends and offer benefits only in the long run through rights issue, bonus issue etc.

Balanced funds are considered moderate since investors seek growth and stability but with moderate risk. Such funds invest both in bonds and blue chip shares. While bonds give stable interest income, the share dividends will be fluctuated though in the long run, they may give larger benefits. The exact balance between the two asset classes namely - shares and bonds depends on the fund managers ability to take risk and his priority for return. The normal ratio between stocks and bonds is 55:45 but if the fund manager is aggressive he could choose a larger equity component.

Income funds are regarded as conservative since investors want regular income and can not wait for more than short to medium term.

Money market funds are regarded as high liquidity oriented as investors attach more value for safety and liquidity.

Sector funds invest only in shares of companies belonging to a specific industry. These funds perform well so long as the industry or the sector is in the upswing, but the risk could be high, if the industry or the sector goes down.

OFFER DOCUMENT OF MUTUAL FUND SCHEMES

The Offer Document shall have two parts i.e. Scheme Information Document (SID) and Statement of Additional Information (SAI). SID shall incorporate all information pertaining to a particular scheme. SAI shall incorporate all statutory information on Mutual Fund. The Mutual Funds shall prepare SID and SAI in the prescribed formats. Contents of SID and SAI shall follow the same sequence as prescribed in the format. The Board of the AMC and the Trustee(s) shall exercise necessary due diligence, ensuring that the SID/SAI and the fees paid are in conformity with the Mutual Funds Regulations. All offer documents (ODs) of Mutual Fund schemes shall be filed with SEBI in terms of the Regulations. For the schemes launched in the first half of a financial year, the SID shall be updated within 3 months from the end of the financial year. However, for the schemes launched in the second half of a financial year, SID shall be updated within 3 months of the end of the subsequent financial year.

For example, for a scheme launched in May, 2015, the SID shall be updated by June 30, 2015 and for a scheme launched in December 2015, the SID shall be updated by June 30, 2016. Thereafter, the SID shall be updated once every year.

ADDITIONAL MODE OF PAYMENT THROUGH APPLICATIONS SUPPORTED BY BLOCKED AMOUNT IN MUTUAL FUNDS

ASBA facility which investors have been enjoying for subscription to public issue of equity capital of companies has been extended to the investors subscribing to New Fund Offers (NFOs) of mutual fund schemes. It shall co-exist with the current process, wherein cheques/ demand drafts are used as a mode of payment. The banks which are in SEBI's list shall extend the same facility in case of NFOs of mutual fund schemes to all eligible investors in Mutual Fund units. Mutual Funds shall ensure that adequate arrangements are made by Registrar and Transfer Agents for the implementation of ASBA. Mutual Funds/AMCs shall make all relevant disclosures in this regard in the SAI. The Mutual Funds/AMCs have to compulsorily provide ASBA facility to the investors for all the NFOs launched by them.

RISKS INVOLVED IN MUTUAL FUNDS

Mutual funds may face the following risks, leading to non-satisfactory performance:

1. Excessive diversification of portfolio, losing focus on the securities of the key segments.
2. Too much concentration on blue-chip securities which are high priced and which do not offer more than average return.
3. Necessity to effect high turnover through liquidation of portfolio resulting in large payments of brokerage and commission.
4. Poor planning of investment with minimum returns.
5. Unresearched forecast on income, profits and Government policies.
6. Fund managers being unaccountable for poor results.
7. Failure to identify clearly the risk of the scheme as distinct from risk of the market.

CALCULATION OF NET ASSET VALUE (NAV)

Mutual funds raise money by selling their shares to public and redeeming them at current net asset value. Net asset value is the value of the assets of each unit of the scheme. Thus if the NAV is the more than the face value of ₹ 10/-, there is an appreciation for the investment. If the NAV is less than the face value, it indicates depreciation of the investment. NAV also includes dividends, interest accruals and reduction of liabilities and expenses apart from market value of investments. Every mutual fund shall compute the NAV of each scheme by dividing the net asset of the scheme by the number of units of that scheme outstanding on the date of

valuation and public the same at least in two daily newspapers at intervals not exceeding one week. However, the net asset value of any scheme for special target segment or any monthly scheme which are not mandatorily required to be listed in the stock exchange may publish the NAV at monthly or quarterly intervals as permitted by SEBI.

MUTUAL FUND COSTS

There are two broad categories of mutual fund costs, namely - (a) Operating expenses (b) Sales charges. These terms are explained below:

- (a) **Operating Expenses:** Costs incurred in operating mutual funds include advisory fees paid to investment managers, custodial fees, audit fees, transfer agent fees, trustee fees, agents commission etc. The break-up of these expenses is required to be reported in the schemes offer document.
- (b) **Sales Charges:** These are otherwise called as sales loads and are charged directly to the investors. Mutual funds use the sales loads for payment of agents commission and expenses for distribution and marketing.

There is no entry load for all mutual fund schemes. The scheme application forms carry a suitable disclosure to the effect that the upfront commission to distributors will be paid by the investor directly to the distributor, based on his assessment of various factors including the service rendered by the distributor. Of the exit load or Contingent Deferred Sales charges (CDSC) charged to the investor, a maximum of 1% of the redemption proceeds is required to be maintained in a separate account which can be used by the AMC to pay commissions to the distributor and to take care of other marketing and selling expenses. Any balance shall be credited to the scheme immediately. CDSC is a structured back end load paid when the units are redeemed during the initial of ownership. The distributors should disclose all the commissions (in the form of trail commission or any other mode) payable to them for the different competing schemes of various mutual funds from amongst which the scheme is being recommended to the investor. AMC(s) shall not charge entry/or exit load on bonus units and units allotted on reinvestment of dividend.

TRANSACTION CHARGES

- A transaction charges means trading expenses charged to the investor when buying or selling units of mutual funds or Exchange Traded Funds (ETFs). A transaction charges per subscription of Rs.10, 000/- and above be allowed to be paid to the distributors of the Mutual Fund products. However, there shall be no transaction charges on direct investments.
- The transaction charge in case of existing investors in a Mutual Fund, the distributor may be paid Rs.100/- as transaction charge per subscription of Rs.10,000/- and above. There shall be no transaction charge on subscription below Rs.10,000/- and in case of new investors, the distributor may be paid Rs.150/- as transaction charge for a first time investor in Mutual Funds.
- The transaction charges, if any, shall be deducted by the AMC from the subscription amount and paid to the distributor; and the balance shall be invested. In case of Systematic Investment Plans (SIPs), the transaction charge shall be applicable only if the total commitment through SIPs amounts to Rs.10,000/- and above. In such cases the transaction charge shall be recovered in 3-4 instalments.

ROLL OVER OF A SCHEME

A mutual fund can roll over a close ended scheme on or before the redemption of the scheme after giving an option to investors to redeem their units at NAV based price. The roll over scheme may include a fresh extension of period or continue under the same terms of the original scheme with or without modifications.

SWITCH OVER ONE SCHEME TO ANOTHER

A mutual fund may use its discretion to permit switching over of the investment in units from one to another of its schemes, to help the investor shift, from a high risk scheme to a low risk one or vice-versa.

ANNUALISED RETURNS

Investors buy and sell mutual fund shares/units during a short period and make profits. Percentage of profits in such short periods can not be a reliable measure. The proper method is to calculate returns on an annualised basis at the compounded average rate over a year.

ASSET MANAGEMENT COMPANY (AMC)

Under SEBI Regulations, every mutual fund is required to have an Asset Management Company (AMC) incorporated in accordance with the Companies Act, 2013 to manage the funds of the mutual fund. The AMC should be approved by SEBI and should enter into an agreement with the trustees of the mutual fund to formulate schemes, raise money against units, invest the funds in accrued securities and after meeting the permissible costs as per norms, distribute income to the share holders of the funds.

RESTRICTION ON REDEMPTION IN MUTUAL FUNDS

The facility of restriction on redemption under any scheme of the mutual fund can be made only after the approval from the board of directors of the Asset Management Company (AMC) and the trustees.

Restriction on redemption should apply during excess redemption requests that could arise in overall market crisis situations rather than exceptional circumstances of entity specific situations.

Therefore, in order to bring more clarity and to protect the interest of the investors, the following requirement shall be observed before imposing restriction on redemptions:

- Restriction may be imposed when there are circumstances leading to a systemic crisis or event that severely constricts market liquidity or the efficient functioning of markets such as:
 - a) Liquidity issues** - When market at large, becomes illiquid affecting almost all securities instead of any issuer specific security. AMCs should have in place, a sound internal liquidity management tools for schemes. Restriction on redemption cannot be used as an ordinary tool in order to manage the liquidity of a scheme.
 - b) Market failures, exchange closures** - When markets are affected by unexpected events which impact the functioning of exchanges or the regular course of transactions. Such unexpected events could also be related to political, economic, military, monetary or other emergencies.
 - c) Operational issues** – When exceptional circumstances are caused by force majeure, unpredictable operational problems and technical failures (e.g. a black out). Such cases can only be considered if they are reasonably unpredictable and occur in spite of appropriate diligence of third parties, adequate and effective disaster recovery procedures and systems.
- Restriction on redemption may be imposed for a specified period of time which is not more than 10 working days in any 90 days period.
- Any imposition of restriction would require specific approval of board of AMCs and trustees and the same should be informed to SEBI immediately.
- When restriction on redemption is imposed, the following procedure shall be applied:
 - a) No redemption requests upto INR 2 lakh shall be subject to such restriction.

- b) Where redemption requests are above INR 2 lakh, AMCs shall redeem the first INR 2 lakh without such restriction and remaining part over and above INR 2 lakh shall be subject to such restriction.

The above information to investors shall be disclosed prominently and extensively in the scheme related documents regarding the possibility that their right to redeem may be restricted in such exceptional circumstances and the time limit for which it can be restricted.

SEBI (MUTUAL FUND) REGULATIONS, 1996

These regulations may be called SEBI (Mutual Funds) Regulations, 1996.

IMPORTANT DEFINITIONS

- **Advertisement** shall include all forms of communication issued by or on behalf of the asset management company/mutual fund that may influence investment decisions of any investor/prospective investors.
- **Asset Management Company** means a company formed and registered under the Companies Act, 2013 and approved as such by SEBI under Regulation 21(2).
- **Mutual Fund** means a fund established in the form of a trust to raise monies through the sale of units to the public or a section of the public under one or more schemes for investing in securities including money market instruments or gold or gold related instruments or real estate assets.
However, infrastructure debt fund schemes may raise monies through private placement of units, subject to conditions specified in these regulations.
- **Money Market Mutual Fund** means a scheme of a mutual fund, set up with the objective of investing exclusively in money market instruments.
- **Sponsor** means any person who, acting alone or in combination with another body corporate establishes a mutual fund.
- **Trustees** mean the Board of Trustees or the Trustee Company who hold the property of the mutual fund in trust for the benefit of the unit holders.
- **Unit** means the interest of the unit holders in a scheme which consists of each unit representing one undivided share in the assets of a scheme.
- **Unit Holder** means a person holding unit in a scheme of a mutual fund.
- **Close-ended scheme** means any scheme of a mutual fund in which the period of maturity of scheme is specified.
- **Open-ended scheme** means a scheme of a mutual fund which offers units for sale without specifying any duration for redemption.
- **Gold exchange traded fund** scheme means a mutual fund scheme that invests primarily in gold or gold related instruments.
- **Gold related instrument** means such instrument having gold as underlying, as may be specified by SEBI from time to time.
- **Capital protection oriented scheme** means a mutual fund scheme which is designated as such and which endeavours to protect the capital invested therein through suitable orientation of its portfolio structure.
- **Index fund scheme** means a mutual fund schemes that invests in securities in the same proportions as an index of securities.

ELIGIBILITY CRITERIA

Regulation 7 lays down the following eligibility criteria to be fulfilled by an applicant to get a certificate of registration. In the opinion of SEBI the applicant should be a fit and proper person. The other criteria are:

- (a) the sponsor should have a sound track record and general reputation of fairness and integrity in all his business transactions.

The regulations provide that "Sound track record" means the sponsor should –

- (i) be carrying on business in financial services for a period of not less than five years; and
- (ii) the networth is positive in all the immediately preceding five years; and
- (iii) the networth in the immediately preceding year is more than the capital contribution of the sponsor in the asset management company; and
- (iv) the sponsor has profits after providing for depreciation, interest and tax in three out of the immediately preceding five years, including the fifth year;

- (aa) the applicant is a fit and proper person;

- (b) in the case of an existing mutual fund, such fund is in the form of a trust and the trust deed has been approved by SEBI;

- (c) the sponsor has contributed or contributes at least 40% to the networth of the asset management company;

However, any person who holds 40% or more of the net worth of an asset management company shall be deemed to be a sponsor and will be required to fulfil the eligibility criteria specified in these regulations;

- (d) the sponsor or any of its directors or the principal officer to be employed by the mutual fund should not have been guilty of fraud or has not been convicted of an offence involving moral turpitude or has not been found guilty of any economic offence;
- (e) appointment of trustees to act as trustees for the mutual fund in accordance with the provisions of the regulations;
- (f) appointment of asset management company to manage the mutual fund and operate the scheme of such funds in accordance with the provisions of these regulations;
- (g) appointment of custodian in order to keep custody of the securities or gold and gold related instrument or other assets of the mutual fund held in terms of these regulations, and provide such other custodial services as may be authorised by the trustees.

TERMS AND CONDITIONS OF REGISTRATION

Regulation 10 lays down that the registration granted to a mutual fund is subject to the following terms and conditions:

- (a) the trustees, the sponsor, the asset management company and the custodian comply with the provisions of these regulations;
- (b) the mutual fund to inform SEBI, if any information or particulars previously submitted to SEBI was misleading or false in any material respect;
- (c) the mutual fund to inform SEBI, of any material change in the information or particulars previously furnished, which have a bearing on the registration granted by it;
- (d) payment of the fees as specified in the regulation and the second schedule.

CONSTITUTION AND MANAGEMENT OF MUTUAL FUND AND OPERATION OF TRUSTEES

Regulation 14 stipulates that a mutual fund shall be constituted in the form of a trust and the instrument of trust shall be in the form of a deed, duly registered under the provisions of Indian Registration Act, 1908 and executed by the sponsor in favour of the trustees named in such instrument.

Regulation 15 lays down that the trust deed shall not contain such clause which has the effect of limiting or extinguishing the obligations and liabilities of the trusts in relation to any mutual fund or the unit holders or indemnifying the trustees or the asset management company for loss or damage caused to the unit holders by their acts of negligence, commission or omission.

CONTENTS OF THE TRUST DEED

The Third Schedule prescribing the contents of the trust deed is reproduced below:

1. (i) A trustee in carrying out his responsibilities as a member of the Board of Trustees or of trustee company, shall maintain arms' length relationship with other companies, or institutions or financial intermediaries or any body corporate with which he may be associated.
 (ii) No trustee shall participate in the meetings of the Board of Trustees or trustee company when any decision for investments in which he may be interested are taken.
 (iii) All the trustees shall furnish to the board of trustees or trustee company particulars of interest which he may have in any other company, or institution or financial intermediary or any corporate by virtue of his position as director, partner or with which he may be associated in any other capacity.
2. Minimum number of trustees must be mentioned in the Trust Deed.
3. The trust deed must provide that the trustees shall take into their custody, or under their control all the property of the schemes of the mutual fund and hold it in trust for the unit holders.
4. The trust deed must specifically provide that unit holders would have beneficial interest in the trust property to the extent of individual holding in respective schemes only.
5. The trust deed shall provide that it would be the duty of the trustees to act in the interest of the unit holders.
6. The trust deed shall provide that it is the duty of trustees to provide or cause to provide information to unit holders and SEBI as may be specified by SEBI.
7. The trust deed shall provide that the trustees shall appoint an AMC approved by SEBI, to float schemes for the mutual fund after approval by the trustees and SEBI, and manage the funds mobilised under various schemes, in accordance with the provisions of the trust deed and regulations. The trustees shall enter into an Investment Management Agreement with the AMC for this purpose, and shall enclose the same with the trust deed.
8. The trust deed shall provide for the duty of the trustee to take reasonable care to ensure that the funds under the schemes floated by and managed by the AMC are in accordance with the Trust Deed and Regulations.
9. The trust deed must provide for the power of the trustees to dismiss the AMC under the specific events only with the approval of SEBI in accordance with the Regulations.
10. The trust deed shall provide that the trustees shall appoint a custodian and shall be responsible for the supervision of its activities in relation to the mutual fund and shall enter into a Custodian Agreement with the custodian for this purpose.

11. The trust deed shall provide that the auditor for the mutual fund shall be different from the auditor of the AMC.
12. The trust deed shall provide for the responsibility of the trustees to supervise the collection of any income due to be paid to the scheme and for claiming any repayment of tax and holding any income received in trust for the holders in accordance with the Trust Deed Regulations.
13. Board policies regarding allocation of payments to capital or income must be indicated in the Trust Deed.
14. The trust deed shall also explicitly forbid the acquisition of any asset out of the trust property which involves the assumption of any liability which is unlimited or shall not result in encumbrance of the trust property in any way.
15. The trust deed shall forbid the mutual fund to make or guarantee loans or take up any activity not in contravention of the Regulations.
16. Trusteeship fee, if any, payable to trustee shall be provided in the Trust Deed.
17. The trust deed shall provide that no amendment to the Trust Deed shall be carried out without the prior approval of the SEBI or unit holders.

However in case a Board of trustees is converted into a trustee company subsequently such conversion shall not require the approval of unit holders.

18. The removal of the trustee in all cases would require the prior approval of SEBI.
19. The trust deed shall lay down the procedure for seeking approval of the unit holders under such circumstances as are specified in the Regulations.
20. The trust deed shall state that a meeting of the trustees shall be held at least once in every two calendar months and at least six such meetings shall be held in every year.
21. The trust deed shall specify the quorum for a meeting of the trustees.

However the quorum for a meeting of the trustees shall not be constituted unless one independent trustee or director is present at the meeting.
22. The trust deed shall state that the minimum number of trustees shall be four.

DISQUALIFICATION FROM BEING APPOINTED AS TRUSTEES

Regulation 16 lays down the attributes of a person to be appointed as trustee. A mutual fund shall appoint trustees in accordance with these regulations. A person shall not be eligible to be appointed as trustees unless –

- (a) he should be a person of ability, integrity and standing;
- (b) he has not been found guilty of moral turpitude;
- (c) he has not convicted of any economic offence or violation of any securities laws and has furnished particulars as required in the prescribed form;
- (d) an asset management company or any of its directors including independent directors, officers or employees shall not be eligible to act as a trustee of any mutual fund;
- (e) a person already appointed as a trustee of a mutual fund can not be appointed again as a trustee of any other mutual fund;
- (f) 2/3 of the trustees shall be independent persons and not associated with the sponsors in any manner, whatsoever;

- (g) where the companies appointed as trustee, then its directors can act as trustees of any other trust provided that the object of the trust is not in conflict with the object of the mutual fund; and
- (h) prior approval of SEBI shall be necessary for the appointment of any trustee.

RIGHTS AND OBLIGATIONS OF TRUSTEES

Regulation 18 lays down the following rights and obligations for the trustees:

- (1) The trustees and the AMC shall with the prior approval of SEBI enter into an investment management agreement.
- (2) Such agreement shall contain all the clauses as prescribed in these Regulations or as well as other clauses necessary for the purpose of making investments; The fourth schedule contains clauses which are to be included as contents of the investment management agreement.
- (3) The trustees are entitled to obtain from the AMC all the information which the trustees consider necessary;
- (4) The trustees shall ensure before the launch of any scheme that the asset management company has –
 - (a) systems in place for its back office, dealing room and accounting;
 - (b) appointed all key personnel including fund manager(s) for the scheme(s) and submitted their bio-data which shall contain the educational qualification, past experience in the securities market with the trustees, within 15 days of their appointment;
 - (c) appointed auditors to audit its accounts;
 - (d) appointed a compliance officer who shall responsible for monitoring the compliance of the Act, rules and regulations, notifications, guidelines, instructions etc. issued by SEBI or the Central Government and for redressal of investors grievances.
 - (e) appointed registrars and laid down parameters for their supervision;
 - (f) prepared a compliance manual and designed internal control mechanisms including internal audit systems;
 - (g) specified norms for empanelment of brokers and marketing agents;
 - (h) obtained, wherever required under these regulations, prior in-principle approval from the recognised stock exchange(s) where units are proposed to be listed.
- (5) The compliance officer appointed under clause (d) of sub-regulation (4) shall in immediately and independently report to SEBI for any non-compliance observed by him.
- (6) The trustees shall ensure that the asset management company (AMC) has been diligent in empaneling the brokers, in monitoring the securities transactions with brokers and avoiding undue concentration of business with any broker;
- (7) The trustees shall ensure the AMC has not given any undue or unfair advantage to any associate or dealt with any of the associates of the AMC in a manner detrimental to the interest of the unit holders;
- (8) The trustees shall ensure that the transaction entered into by the AMC or in accordance with these regulations and the mutual fund scheme concerned;
- (9) The trustees shall ensure that the AMC has been managing the mutual fund schemes independently of other activities and have taken adequate steps to ensure that the interest of the investors of one scheme are not being compromised with those of any other scheme or of other activities of the AMC;

(10) The trustees shall ensure that all the activities of the AMC are in accordance with the provisions of these regulations;

(11) Where the trustees have reason to believe that the conduct of business of the mutual fund is not in accordance with these regulations and the scheme, they shall forthwith take such remedial steps as are necessary by them and shall immediately inform SEBI of the violation and the action taken by them;

(12) Each trustee shall file the details of his transactions of dealing in securities with a mutual fund on a quarterly basis;

(13) The trustees shall be accountable for and be the custodian of the funds and the property of the respective schemes and shall hold the same in trusts for the benefit of the unitholders in accordance with these regulations and the trust deed;

(14) The trustees shall take steps to ensure that the transactions of the mutual fund are in accordance with the provisions of the trust deed;

(15) The trustees shall be responsible for the calculation of any income due to be paid to the mutual fund and also of any income received in the mutual fund for the holders of the unit of any scheme in accordance with these regulations and the trust deed;

(16) The trustees shall obtain the consent of the unit holders –

- (a) whenever required to do so by SEBI in the interest of the unit holders; or
- (b) whenever required to do so on the requisition of 3/4 of the unit holders of any scheme; or
- (c) when the majority of the trustees decide to wind up or pre-maturely redeem the units;

(17) The trustees shall ensure that no change in the fundamental attributes of any scheme or the trust or fees and expenses payable or any other change which would modify the scheme and affects the interest of unit holders, shall be carried out unless, -

- (i) a written communication about the proposed change is sent to each unit holder and an advertisement is given in one English daily newspaper having nationwide circulation as well as in a newspaper published in the language of the region where the Head Office of the mutual fund is situated; and
- (ii) the unit holders are given an option to exit at the prevailing Net Asset Value without any exit load;

(18) The trustees shall on a quarterly basis review all transactions carried out between the mutual funds, AMC and its associates and also the networth of the AMC. In case of any short fall in the networth the trustees shall ensure that the AMC make up for the short fall;

(19) The trustees shall periodically review all service contracts such as custody arrangements, transfer agency of the securities and satisfy itself that they are executed in the interest of the unit holders. Similarly, the trustees shall periodically review the investor complaints received and ensure redressal of the same by the AMC;

(20) The trustees shall ensure that there is no conflict of interest between the manner of deployment of its networth by the asset management company and the interest of the unit-holders.

(21) The trustees shall furnish to SEBI on a half yearly basis –

- (a) a report on the activities of the mutual fund;
- (b) a certificate stating that the trustees have satisfied themselves that there have been no instances of self dealing or front running by any of the trustees, directors or key personnel of the AMC.
- (c) a certificate that the trustees have not found any instances of self dealing or front running by any of the trustees, directors or key personnel of the AMC and a certificate to the effect that the AMC has been managing the schemes independently of any other activities and protecting the interest of the unit holders.

(22) The independent trustees shall give their comments on the report of the AMC as regards investments by the mutual fund in the securities of group companies of the sponsor.

(23) The trustees shall abide by the code of conduct as specified in the Fifth Schedule.

CODE OF CONDUCT FOR MUTUAL FUNDS

- (a) Mutual fund schemes should not be organised, operated, managed or the portfolio of securities selected, in the interest of sponsors, directors of AMCs, members of Board of trustees or directors of trustee company, associated persons as in the interest of special class of unit holders rather than in the interest of all classes of unit holders of the scheme.
- (b) Trustees and AMCs must ensure the dissemination to all unit holders of adequate, accurate, explicit and timely information fairly presented in a simple language about the investment policies, investment objectives, financial position and general affairs of the scheme.
- (c) Trustees and AMCs should avoid excessive concentration of business with broking firms, affiliates and also excessive holding of units in a scheme among a few investors.
- (d) Trustees and AMCs must avoid conflicts of interest in managing the affairs of the schemes and keep the interest of all unit holders paramount in all matters.
- (e) Trustees and AMCs must ensure schemewise segregation of bank accounts and securities accounts.
- (f) Trustees and AMCs shall carry out the business and invest in accordance with the investment objectives stated in the offer documents and take investment decision solely in the interest of unit holders.
- (g) Trustees and the AMC shall maintain high standards of integrity and fairness in all their dealings and in the conduct of their business.
- (h) Trustees and AMC must not use any unethical means to sell; market or induce any investor to buy their schemes.
- (i) Trustees and the AMC shall render at all times high standard of service, exercise due diligence, ensure proper care and exercise independent professional judgment.
- (j) The AMC shall not make any exaggerated statement, whether oral or written, either about their qualifications or capability to render investment management services or their achievements.
- (k) (a) The sponsor of the mutual fund, the trustees or the asset management company and any of their employees shall not render, directly or indirectly any investment advice about any security in the publicity accessible media, whether real time or non-real-time, unless a disclosure of his interest including long or short position in the said security has been made, while rendering such advice.
 (b) In case, an employee of the sponsor, the trustees or the asset management company is rendering such advice, he shall also disclose the interest of his dependent family members and the employer including their long or short position in the said security, while rendering such advice.

GENERAL DUE DILIGENCE AND SPECIFIC DUE DILIGENCE BY TRUSTEES

The trustees shall exercise due diligence as under:

(A) General Due Diligence:

- (i) the trustees shall be discerning in the appointment of the directors on SEBI of the asset management company.
- (ii) trustees shall review the desirability on continuance of the asset management company if substantial

irregularities are observed in any of the schemes and shall not allow the asset management company to float new schemes.

- (iii) the trustee shall ensure that the trust property is properly protected, held and administered by proper persons and by a proper number of such persons.
- (iv) the trustee shall ensure that all service providers are holding appropriate registrations from SEBI or concerned regulatory authority.
- (v) the trustees shall arrange for test checks of service contracts.
- (vi) trustees shall immediately report to SEBI of any special developments in the mutual fund.

(B) Specific Due Diligence:

The trustees shall:

- (i) obtain internal audit reports at regular intervals from independent auditors appointed by the trustees;
- (ii) obtain compliance certificate at regular intervals from the asset management company;
- (iii) hold meeting of trustee more frequently;
- (iv) consider the reports of the independent auditor and compliance reports of asset management company at the meetings of trustees for appropriate action;
- (v) maintain records of the decisions of the trustees at their meetings and of the minutes of the meetings;
- (vi) prescribe and adhere to a code of ethics by the trustees, asset management company and its personnel;
- (vii) communicate in writing to the asset management company of the deficiencies and checking on the rectification of deficiencies.

INDEPENDENT DIRECTORS' RESPONSIBILITIES

The independent directors of the trustees or the AMC shall pay specific attention to the following:

- (1) the Investment Management Agreement and the compensation paid under the agreement,
- (2) service contracts with affiliates – whether the asset management company has charged higher fees than outside contractors for the same services,
- (3) selections of the asset management company's independent directors,
- (4) securities transactions involving affiliates to the extent such transactions are permitted,
- (5) selecting and nominating individuals to fill independent directors vacancies,
- (6) code of ethics must be designed to prevent fraudulent, deceptive or manipulative practices by insiders in connection with personal securities transactions,
- (7) the reasonableness of fees paid to sponsors, asset management company and any others for services provided,
- (8) principal underwriting contracts and their renewals,
- (9) any service contract with the associates of the asset management company.

PROCEDURE FOR LAUNCHING OF SCHEMES

- A scheme shall not be launched by the asset management company unless such scheme is approved by the trustees and a copy of the offer document has been filed with SEBI.
- The mutual fund shall pay the minimum filing fee and balance filing fee calculated in accordance with the Second Schedule to SEBI while filing the offer document.

- The sponsor or asset management company shall invest not less than one percent of the amount which would be raised in the new fund offer or fifty lakh rupees, whichever is less, in the growth option of the scheme and such investment shall not be redeemed unless the scheme is wound up. However, this shall not apply to close ended schemes.

ADVERTISEMENTS CODE FOR MUTUAL FUNDS

Advertisements shall be in accordance with the advertisement code specified in the Sixth Schedule and shall be submitted to SEBI within 7 days from the date of their issue.

The Advertisement code prescribes for the following :

- Advertisements shall be accurate, true, fair, clear, complete, unambiguous and concise.
- Advertisements shall not contain statements which are false, misleading, biased or deceptive, based on assumption/projections and shall not contain any testimonials or any ranking based on any criteria.
- Advertisements shall not be so designed as likely to be misunderstood or likely to disguise the significance of any statement. Advertisements shall not contain statements which directly or by implication or by omission may mislead the investor.
- Advertisements shall not carry any slogan that is exaggerated or unwarranted or slogan that is inconsistent with or unrelated to the nature and risk and return profile of the product.
- No celebrities shall form part of the advertisement.
- Advertisements shall not be so framed as to exploit the lack of experience or knowledge of the investors. Extensive use of technical or legal terminology or complex language and the inclusion of excessive details which may detract the investors should be avoided.
- Advertisements shall contain information which is timely and consistent with the disclosures made in the Scheme Information Document, Statement of Additional Information and the Key Information Memorandum.
- No advertisement shall directly or indirectly discredit other advertisements or make unfair comparisons.
- Advertisements shall be accompanied by a standard warning in legible fonts which states, Mutual Fund investments are subject to market risks, read all scheme related documents carefully. No addition or deletion of words shall be made to the standard warning.
- In audio-visual media based advertisements, the standard warning in visual and accompanying voice over reiteration shall be audible in a clear and understandable manner. For example, in standard warning both the visual and the voice over reiteration containing 14 words running for at least 5 seconds may be considered as clear and understandable.

IN PRINCIPLE APPROVAL FROM RECOGNISED STOCK EXCHANGE(S)

The listed entity which intends to list units of its scheme on the recognised stock exchange(s), shall obtain 'in-principle' approval from recognised stock exchange(s) in the manner as specified by the recognised stock exchange(s) from time to time.

LISTING AGREEMENT

Every mutual fund desirous of listing units of its schemes on a recognised stock exchange shall execute an agreement with such stock exchange.

Every mutual fund which has previously entered into agreements with a recognised stock exchange to list units of its schemes shall execute a fresh listing agreement with such stock exchange within six months of the date of

notification of Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015.

LISTING OF CLOSE ENDED SCHEME

Regulation 32 lays down that every close ended scheme other than an equity linked saving scheme shall be listed in a recognised stock exchange within such time period and subject to condition as specified by SEBI.

However, listing of close ended scheme shall not be mandatory –

- (a) if the said scheme provides for periodic repurchase facility to all the unit holders with restriction, if any, on the extent of such repurchase; or
- (b) if the said scheme provides for monthly income or caters to special classes of persons like senior citizens, women, children, widows or physically handicapped or any special class of persons providing for repurchase of units at regular intervals; or
- (c) if the details of such repurchase facility are clearly disclosed in the offer document; or
- (d) if the said scheme opens for repurchase within a period of six months from the closure of subscription; or
- (e) if the said scheme is a capital protection oriented scheme.

REPURCHASE OF CLOSE ENDED SCHEME

Regulation 33 says that Units of a close ended scheme, other than those of an equity linked savings scheme, shall not be repurchased before the end of maturity period of such scheme.

The units of close ended schemes may be open for sale or redemption at fixed predetermined intervals if the maximum and minimum amount of sale or redemption of the units and the periodicity of such sale or redemption have been disclosed in the offer document.

It also permits conversion of close ended scheme into open ended scheme subject to specified conditions, otherwise a close ended scheme shall be fully redeemed at the end of the maturity period. The conditions which are required to comply for the conversion of close ended scheme into open ended scheme are as follows:-

- (a) if the offer document of such scheme discloses the option and the period of such conversion; or
- (b) the unit holders are provided with an option to redeem their units in full
- (c) the initial issue expenses of the scheme have been amortized fully in accordance with the Tenth Schedule.

A close-ended scheme may be allowed to be rolled over if the purpose, period and other terms of the roll over and all other material details of the scheme including the likely composition of assets immediately before the roll over, the net assets and net asset value of the scheme, are disclosed to the unitholders and a copy of the same has been filed with SEBI.

Further, such roll over will be permitted only in the case of those unitholders who express their consent in writing and the unitholders who do not opt for the roll over or have not given written consent shall be allowed to redeem their holdings in full at net asset value based price.

OFFERING PERIOD

Regulation 34 lays down that no scheme of mutual fund other than an initial offering of equity linked savings scheme shall be open for subscription for more than 15 days. However, in case of mutual fund schemes eligible under Rajiv Gandhi Equity Saving Scheme, the period specified in these regulations shall not be more than thirty days.

ALLOTMENT OF UNITS AND REFUND OF MONEY

- Regulation 35 lays down that the Asset Management Company shall specify in the offer document:
 - (a) the minimum subscription amount it seeks to raise under the scheme; and
 - (b) in case of oversubscription the extent of subscription it may retain . However, where the asset management company retains the oversubscription, all the applicants applying up to five thousand units shall be given full allotment subject to the oversubscription mentioned in clause (b).
- The mutual fund and Asset Management Company shall be liable to refund the application money to the applicants:
 - (i) if the mutual fund fails to receive the minimum subscription amount ;
 - (ii) if the moneys received from the applicants for units are in excess of subscription .
- Any amount refundable shall be refunded within a period of five working days from the date of closure of subscription list, by Registered post with acknowledgement due and by cheque or demand draft marked “A/c payee” to the applicants. However, in case of mutual fund schemes eligible under Rajiv Gandhi Equity Savings Scheme, the period shall be fifteen days from the closure of the initial subscription list.
- In the event of failure to refund the amounts within the period specified the asset management company shall be liable to pay interest to the applicants at a rate of fifteen per cent per annum from the expiry of five working days from the date of closure of the subscription list.

However, in case of mutual fund schemes eligible under Rajiv Gandhi Equity Savings Scheme, the period shall be fifteen days from the closure of the initial subscription list.

TRANSFER OF UNITS

Regulation 37 states that a unit is freely transferable except where it is specifically restricted or prohibited under the scheme. A unit holder in a close ended scheme listed on a recognized stock exchange, who desires to trade in units shall hold units in dematerialized form. The asset management company shall, on production of instrument of transfer with relevant unit certificates, register the transfer and return the unit certificate to the transferee within 30 days from the date of such production. However, if the units are with the depository such units will be transferable in accordance with the provisions of SEBI (Depositories and Participants) Regulations, 1996.

GUARANTEED RETURNS

Regulation 38 lays down that no guaranteed return shall be provided in a scheme : -

- (a) unless such scheme fully guaranteed by the sponsor or AMC;
- (b) unless a statement indicating the name of the person who will guarantee the return, is made in the offer document.
- (c) the manner in which the guarantee is to be met has been stated in the offer document.

CAPITAL PROTECTION ORIENTED SCHEMES

Regulation 38A of the Regulations provides that a capital protection oriented scheme may be launched, subject to the following:

- (a) the units of the scheme are rated by a registered credit rating agency from the viewpoint of the ability of its portfolio structure to attain protection of the capital invested therein;
- (b) the scheme is close ended; and

(c) there is compliance with such other requirements as may be specified by SEBI in this behalf.

Regulation 39 to 42 deal with winding up of a close ended scheme on the expiry of its duration, the effect of winding up, the procedure and manner thereof. It is enjoined that trustees shall forward to SEBI and to the unitholders a report on the winding up. On SEBI being satisfied about the completion of all the necessary measures, a scheme shall cease to exist. The units of a mutual fund scheme must delisted from a recognized stock exchange in accordance with the guidelines as may be specified by SEBI.

INVESTMENT OBJECTIVES AND VALUATION POLICIES

Regulation 43 lays down that the monies collected under any scheme of a mutual fund shall be invested only in securities, money market instruments; privately placed debentures; securitised debt instruments which are either asset backed or mortgage backed securities, gold or gold related instruments or real estate assets, infrastructure debt instrument and assets. Investment shall be made in accordance with the investment objective of the relevant mutual fund scheme. However, monies collected under any money market scheme of a mutual fund shall be invested only in money market instruments. Moneys collected under any gold exchange trade fund scheme shall be invested only in gold or gold related instruments, moneys collected under a real estate scheme shall be invested in accordance with Regulation 49E.

Regulation 44 talks about investment, borrowing and connected restrictions. Any investments shall be made subject to the investment restriction specified in the Seventh Schedule to the Regulations which contains 11 clauses. However, seventh schedule does not apply to a gold exchange traded fund scheme.

A mutual fund having an aggregate of securities which are worth Rs. 10 crore or more as on the latest balance sheet date, shall settle their transactions only through dematerialised securities, as per instructions of SEBI. The mutual funds shall not borrow except to meet temporary liquidity needs for the purpose of repurchase, redemption of units or payment of interest or dividend to the unit holders. Such borrowals should not exceed 12% of the net asset value of the scheme and the duration of the borrowing shall not exceed six months. The mutual fund shall not advance any loans for any purpose but may lend securities in accordance with the framework relating to short selling and securities lending and borrowing specified by SEBI.

OVERSEAS INVESTMENT BY MUTUAL FUNDS

Mutual Funds are permitted to make investment in:

- (i) ADRs/ GDRs issued by Indian or foreign companies;
- (ii) Equity of overseas companies listed on recognized stock exchanges overseas;
- (iii) Initial and follow on public offerings for listing at recognized stock exchanges overseas;
- (iv) Foreign debt securities in the countries with fully convertible currencies, short term as well as long term debt instruments with rating not below investment grade by accredited/registered credit rating agencies;
- (v) Money market instruments rated not below investment grade;
- (vi) Repos in the form of investment, where the counterparty is rated not below investment grade; repos should not however, involve any borrowing of funds by mutual funds;
- (vii) Government securities where the countries are rated not below investment grade;
- (viii) Derivatives traded on recognized stock exchanges overseas only for hedging and portfolio balancing with underlying as securities;
- (ix) Short term deposits with banks overseas where the issuer is rated not below investment grade;
- (x) Units/securities issued by overseas mutual funds or unit trusts registered with overseas regulators and investing in (a) aforesaid securities, (b) Real Estate Investment Trusts (REITs) listed in recognized stock exchanges overseas or (c) unlisted overseas securities (not exceeding 10% of their net assets).

Transaction in excess of permissible limits — A case study***SEBI v. Shriram Mutual Fund & Others - Appeal No. 9523-24 of 2003***

- (a) A penalty of Rs.2 lakh was imposed by Adjudicating Officer (AO) on Shriram Mutual Fund (SMF) as it had repeatedly exceeded the permissible limits of transactions through its associate broker, in terms of Regulation 25(7) (a) of SEBI (Mutual Funds) Regulations.
- (b) On an appeal by SMF, SAT vide its final judgment and order dated August 21, 2003, set aside AO's order inter-alia on the ground that the limit was not exceeded intentionally.
- (c) SEBI filed an appeal under Section 15Z of the SEBI Act in the Hon'ble Supreme Court.
- (d) The Hon'ble Supreme Court pronounced its final judgment and order on May 23, 2006. Hon'ble Supreme Court set aside the judgment of SAT and settled the issues, as under:
 - Mens rea is not an essential ingredient for contravention of the provisions of a Civil Act.
 - Penalty is attracted as soon as contravention of the statutory obligation as contemplated by the Act is established, and therefore the intention of the parties committing such violation becomes immaterial.
 - Unless the language of the statute indicated the need to establish the element of mens rea, it is generally sufficient to prove that a default in complying with the statute has occurred.
 - Once the contravention is established, the penalty has to follow and only the quantum of penalty is discretionary.
 - The SAT has erroneously relied on the judgment in the case of Hindustan Steel Limited vs. State of Orissa (AIR 1970 SC 253) as the said case has no application in the present case which relates to imposition of civil liabilities under SEBI Act and Regulations; and is not a criminal / quasi-criminal proceeding.
 - Imputing mens rea into the provisions of Chapter VIA is against the plain language of the statute and frustrates entire purpose and object of introducing Chapter VIA which was to give teeth to the SEBI to secure strict compliance of the Act and the Regulations.

PROHIBITION ON CARRY FORWARD TRANSACTION, DERIVATIVE TRANSACTIONS, SHORT SELLING

Regulation 45 provides that the funds of scheme shall not in any manner be used in carry forward transaction. However, a mutual funds may enter into derivative transactions on a recognised stock exchange, subject to framework specified by SEBI. A mutual fund may enter into short selling transactions on a recognised stock exchange, subject to the framework relating to short selling and securities lending and borrowing specified by SEBI.

UNDERWRITING

Regulation 46 permits mutual funds to enter into underwriting agreement after obtaining a certificate of registration in terms of SEBI Underwriters Rules and SEBI Underwriters Regulations. The Underwriting obligations will be deemed to be investments made in such securities. The capital adequacy norms for the purpose of underwriting shall be the net asset of the scheme. However, the Underwriting obligation of a mutual fund shall not at any time exceed the total NAV of the scheme.

INVESTMENT VALUATION NORMS

Regulation 47 deals with the method of valuation of investments. Every mutual fund shall ensure that the asset management company computes and carries out valuation of investments made by its scheme(s) in accordance

with the investment valuation norms specified in Eighth Schedule, and publishes the same with the valuation norms specified in the Eighth Schedule to the Regulations.

Regulation 48 lays down that every mutual fund shall compute the NAV of each scheme by dividing the net assets of the scheme with a number of units of that scheme outstanding on the valuation date. The Net Asset Value of the scheme shall be calculated on daily basis and published in at least two daily newspapers having circulation all over India.

Regulation 49 deals with pricing of units. The price at which units may be subscribed or sold and the price at which such units may at any time be purchased by the mutual fund shall be made available to the investors. In the case of open ended scheme, the mutual fund shall at least once in a week publish in a daily newspaper of all India circulation, the sale and repurchase price of the units. The funds shall ensure that such repurchase price is not lower than 93% of NAV and the sale price is not higher than 107 per cent of the NAV. The difference between repurchase price and sale price shall not exceed 7 percent calculated on the sale price.

The price of units shall be determined with reference to the last determined NAV, unless the scheme announces the NAV on a daily basis and the sale price is determined with or without a fixed premium added to the future NAV which is declared in advance.

INSTANT ACCESS FACILITY AND USE OF E-WALLET FOR INVESTMENT IN MUTUAL FUNDS

SEBI issued guidelines on Instant Access Facility and Use of e-wallet for investment in Mutual Funds (MFs). Instant Access Facility (IAF) simplifies the credit of redemption proceeds in the bank account of the investor on the same day of redemption request. E- Wallet is an electronic device that allows an individual to make electronic transactions.

GENERAL OBLIGATIONS OF THE MUTUAL FUNDS

Regulation 50 lays down that every AMC for each scheme shall keep and maintain proper books of accounts, records and documents, for each scheme so as to explain its transactions and to disclose at any point of time the financial position of each scheme and in particular, give a true and fair view of the state of affairs of the fund and intimate to SEBI the place where such books of accounts, records and documents are maintained. All these documents shall be preserved by the AMC for a period of 8 years.

The AMC shall follow the accounting policies and standards as specified in Ninth Schedule to provide appropriate details of the scheme-wise disposition of the assets of the fund at the relevant accounting date and the performance during that period together with information regarding distribution or accumulation of income accruing to the unit holder in a fair and true manner.

The asset management company may charge the scheme with investment and advisory fees which shall be fully disclosed in the offer document.

Regulation 52A provides that a mutual fund may declare dividends in accordance with the offer document and subject to such guidelines as may be specified by SEBI.

Regulation 53 lays down that every mutual fund and AMC shall despatch to the unitholders the dividend warrants within 30 days of the declaration of the dividend and despatch the redemption or repurchase proceeds within 10 working days from the date of such redemption or repurchase. If AMC failed to dispatch the redemption or repurchase proceeds within 10 working days from the date of such redemption or repurchase, it shall be liable to pay interest to the unit holders at such rate as may be specified by SEBI for the period of delay. Besides this, the AMC may also be liable for penalty in respect of the delay.

Regulations 54 to 57 deal with the annual report, auditors report, publication thereof and forwarding to SEBI. Every mutual fund or AMC shall prepare in respect of each financial year an annual report and an annual

statement of accounts of the schemes and the fund as specified in these Regulations. Every mutual fund shall have the annual statement of accounts audited by a practising Chartered Accountant who is not in any way associated with the auditor of the AMC. The auditor shall be appointed by the trustees to whom the auditor shall forward his report. It shall be included as part of the annual report of the mutual fund.

Regulation 56 requires that the schemewise Annual Report of a mutual fund or an abridged summary thereof shall be mailed to all unitholders as soon as may be but not later than four months from the date of closure of the relevant accounts year. However, the scheme wise annual report or abridged summary thereof may be sent to investors in electronic form on their registered e-mail address in the manner specified by SEBI. The report mailed in abridged summary form shall carry a note that for unitholder of a scheme full Annual Report shall be available for inspection at the head office of the mutual fund and a copy thereof shall be made available to unitholder on payment of such nominal fees as may be specified by the mutual fund. The asset management company shall display the link of the full scheme wise annual reports prominently on their website.

Regulation 57 requires that every mutual funds shall annual report forward its to SEBI within 4 months from the date of closure of each financial year.

Regulations 58 and 59 indicate the periodical and continual disclosures as well as half yearly disclosures to be made by the mutual fund, AMC and others closely connected to them. Regulation 60 enjoins that the trustee shall be bound to make all essential disclosures to unit holders to keep them informed about any information which may have an adverse bearing on their investments.

DISCLOSURE BY MUTUAL FUNDS

Monthly Portfolio Disclosures	Half Yearly disclosure of Portfolios	Unaudited Half Yearly Financials
<p>Mutual funds/AMCs shall make monthly portfolio disclosures (along with ISIN) as on the last day of the month for all their schemes on their respective website on or before the tenth day of the succeeding month in a user-friendly and downloadable format.</p> <p>The format for monthly portfolio disclosure shall be same as that of half yearly portfolio disclosures. Mutual funds/AMCs may also disclose additional information (such as ratios, etc.) subject to compliance with the Advertisement Code.</p>	<p>Mutual Funds shall send a complete statement of Scheme Portfolio to the unit holders before the expiry of one month from the closure of each half year (i.e. March 31 and September 30), if such statement is not published by way of advertisement.</p> <p>Disclosure of investments in derivative instruments by Mutual Funds in half yearly portfolio disclosure, annual report or in any other disclosures is prescribed.</p> <p>The Scheme Portfolio(s) shall also be disclosed on the Mutual Funds' websites before the expiry of one month from the closure of each half year (i.e. March 31 and September 30) and a copy of the same shall be filed with the SEBI along with the half yearly results.</p>	<p>The half yearly disclosures of the unaudited financial results on respective website should be made in a user-friendly and downloadable format.</p> <p>The publication of the unaudited half-yearly results shall be made in line with provisions of the Regulations, in the format prescribed in Twelfth Schedule.</p>

Note : A mutual fund shall also send a complete statement of its scheme portfolios to all unitholders before the expiry of one month from the close of each half year. However, statement of scheme portfolio may not be sent to the unitholders, if the statement is published, by way of an advertisement, in one English daily circulating in the whole of India and in a newspaper published in the language of the region where the head office of the mutual fund is situated.

INFRASTRUCTURE DEBT FUND SCHEMES

“Infrastructure debt fund scheme” means a mutual fund scheme that invests primarily (minimum 90% of scheme assets) in the debt securities or securitized debt instrument of infrastructure companies or infrastructure capital companies or infrastructure projects or special purpose vehicles which are created for the purpose of facilitating or promoting investment in infrastructure, and other permissible assets in accordance with these regulations or bank loans in respect of completed and revenue generating projects of infrastructure companies or projects or special purpose vehicles.

‘Strategic Investor’ means;

- (i) an Infrastructure Finance Company registered with Reserve Bank of India as Non Banking Financial Company;
- (ii) a Scheduled Commercial Bank;
- (iii) International Multilateral Financial Institution;
- (iv) Systematically important NBFCs registered with RBI;
- (v) FIIs registered with SEBI which are long term investors, subject to their applicable investment limits.

APPLICABILITY

The provisions of chapter VI B of SEBI (Mutual Funds) Regulation, 1996 shall apply to infrastructure debt fund schemes launched by mutual funds.

ELIGIBILITY CRITERIA FOR LAUNCHING INFRASTRUCTURE DEBT FUND SCHEME

- (1) An existing mutual fund may launch an infrastructure debt fund schemes if it has an adequate number of key personnel having adequate experience in infrastructure sector.
- (2) A certificate of registration may be granted to an applicant proposing to launch only infrastructure debt fund schemes if the sponsor or the parent company of the sponsor : –
 - (a) has been carrying on activities or business in infrastructure financing sector for a period of not less than five years;
 - (b) fulfils the eligibility criteria as provided in Regulation 7.

OFFERING PERIOD

A scheme of infrastructure debt fund, in case of a public offer, shall be open for subscription for more than forty five days.

CONDITIONS FOR INFRASTRUCTURE DEBT FUND SCHEMES

(1) An infrastructure debt fund scheme shall be launched either as close-ended scheme maturing after more than five years or interval scheme with lock-in of five years and specified transaction period of not more than forty five days as may be specified in the scheme information document.

However, the tenure of the scheme may be extended to two years subject to approval of two-thirds of the unit holders by value of their investment in the schedule.

- (2) Units of infrastructure debt fund schemes shall be listed on a recognized stock exchange, provided that such units shall be listed only after being fully paid up.
- (3) Mutual Funds may disclose indicative portfolio of infrastructure debt fund scheme to its potential investors disclosing the type of assets the mutual fund will be investing.
- (4) An infrastructure debt fund scheme shall have minimum five investors and no single investor shall hold more than fifty percent of net assets of the scheme.
- (5) No infrastructure debt fund scheme shall accept any investment from any investor which is less than ₹ 1 crore.
- (6) The minimum size of the unit shall be ₹ 10 lakhs.
- (7) Each scheme launched as infrastructure debt fund scheme shall have firm commitment from the strategic investors for contribution of an amount of at least ₹ 25 crores before the allotment of units of the scheme are marketed to other potential investors.
- (8) Mutual Funds launching infrastructure debt fund scheme may issue partly paid units to the investors, subject to following conditions:
 - (a) The asset management company shall call for the unpaid portions depending upon the deployment opportunities;
 - (b) The offer document of the scheme shall disclose the interest or penalty which may be deducted in case of non payment of call money by the investors within stipulated time; and
 - (c) The amount of interest or penalty shall be retained in the scheme.

PRIVATE PLACEMENT

The units of an infrastructure debt fund scheme may be offered through private placement to less than fifty persons, subject to approval by the trustees and the board of the asset management company.

The offer made, shall be subject to the following:

- (a) A placement memorandum, in the manner as specified by SEBI, shall be filed by the mutual fund with SEBI at least seven days prior to the launch of the scheme; and
- (b) the mutual fund shall pay to SEBI, filing fee as specified in the Second Schedule.

PERMISSIBLE INVESTMENTS

- (1) Every infrastructure debt fund scheme shall invest at least ninety percent of the net assets of the scheme in the debt securities or securitized debt instruments of infrastructure companies or projects or special purpose vehicles which are created for the purpose of facilitating or promoting investment in infrastructure or bank loans in respect of completed and revenue generating projects of infrastructure companies or special purpose vehicle.
 However, the funds received on account of repayment of principal, whether by way of pre-payment or otherwise, with respect to the underlying assets of the scheme shall be invested as specified in this regulation. Further, if the investment specified in this sub-regulations are not available such funds may be invested in bonds of public financial institutions and infrastructure finance companies.
- (2) Every infrastructure debt fund scheme may invest the balance amount in equity shares, convertibles including mezzanine financing instruments of companies engaged in infrastructure, infrastructure development projects, whether listed on a recognized stock exchange in India or not; or money market instruments and bank deposits.
- (3) The investment restrictions shall be applicable on the life-cycle of the infrastructure debt fund scheme and shall be reckoned with reference to the total amount raised by the infrastructure debt fund scheme.
- (4) No mutual fund shall, under all its infrastructure debt fund schemes, invest more than thirty per cent of

its net assets in the debt securities or assets of any single infrastructure company or project or special purpose vehicles which are created for the purpose of facilitating or promoting investment in infrastructure or bank loans in respect of completed and revenue generating projects of any single infrastructure company or project or special purpose vehicle.

- (5) An infrastructure debt scheme shall not invest more than 30% of the net assets of the scheme in debt instruments or assets of any single infrastructure company or project or special purpose vehicles which are created for the purpose of facilitating or promoting investment in infrastructure or bank loans in respect of completed and revenue generating projects of any single infrastructure company or project or special purpose vehicle.
- (5A) The overall investments by an infrastructure debt fund scheme in debt instruments or assets of infrastructure companies or projects or special purpose vehicles, which are created for the purpose of facilitating or promoting investment in infrastructure or bank loans in respect of completed and revenue generating projects of infrastructure companies or projects or special purpose vehicles, which are rated below investment grade or are unrated, shall not exceed 30% of the net assets of the scheme:

However, the overall investment limit may increase up to 50% of the net assets of the scheme with the prior approval of the trustees and the board of the asset management company.

- (6) No infrastructure debt fund scheme shall invest in –
- (i) Any unlisted security of the sponsor or its associate or group company;
 - (ii) Any listed security issued by way of preferential allotment by the sponsor or its associate or group company;
 - (iii) Any listed security of the sponsor or its associate or group company or bank loan in respect of completed and revenue generating projects of infrastructure companies or special purpose vehicles of the sponsor or its associate or group companies, in excess of twenty five per cent of the net assets of the scheme, subject to approval of trustees and full disclosures to investors for investments made within the aforesaid limits; or
 - (iv) Any asset or securities owned by the sponsor or asset management company or their associates in excess of 30% of the net assets of the scheme, provided that-
 - (a) such investment is in assets or securities not below investment grade;
 - (b) the sponsor or its associates retains atleast 30% of the assets or securities, in which investment is made by the scheme, till the assets or securities are held in the scheme portfolio; and
 - (c) approval for such investment is granted by the trustees and full disclosures are made to the investors regarding such investment.

VALUATION OF ASSETS AND DECLARATION OF NET ASSET VALUE

- (1) The assets held by an infrastructure debt fund scheme shall be valued “in good faith” by the asset management company on the basis of appropriate valuation methods based on principles approved by the trustees.
- (2) The valuation shall be documented and the supporting data in respect of each security so valued shall be preserved at least for a period of five years after the expiry of the scheme.
- (3) The methods used to arrive at values ‘in good faith’ shall be periodically reviewed by the Trustees and by the statutory auditor of the mutual fund.
- (4) The valuation policy approved by the board of asset management company shall be disclosed in the scheme information document.
- (5) The net asset value of every infrastructure debt fund scheme shall be calculated and declared atleast once in each quarter.

DUTIES OF ASSET MANAGEMENT COMPANY

- (1) The asset management company shall lay down an adequate system of internal controls and risk management.
- (2) The asset management company shall exercise due diligence in maintenance of the assets of an infrastructure debt fund scheme and shall ensure that there is no avoidable deterioration in their value.
- (3) The asset management company shall record in writing, the details of its decision making process in buying or selling infrastructure companies' assets together with the justifications for such decisions and forward the same periodically to trustees.
- (4) The asset management company shall ensure that investment of funds of the Infrastructure Debt Fund schemes is not made contrary to provisions of this chapter and the trust deed.
- (5) The asset management company shall obtain, wherever required under these regulations, prior in-principle approval from the recognized stock exchange(s) where units are proposed to be listed.
- (6) The asset management company shall institute such mechanisms as to ensure that proper care is taken for collection, monitoring and supervision of the debt assets by appointing a service provider having extensive experience thereof, if required.

DISCLOSURES IN OFFER DOCUMENT AND OTHER DISCLOSURES

1. The offer documents of infrastructure debt fund schemes shall contain disclosures which are adequate for investors to make informed investment decisions and such further disclosures as may be specified by SEBI.
2. The portfolio disclosures and financial results in respect of an infrastructure debt fund schemes shall contain such further disclosures as may be specified by SEBI.
3. Advertisements in respect of infrastructure debt fund schemes shall conform to such guidelines as may be specified by SEBI.

TRANSACTIONS BY EMPLOYEES ETC.

1. All transactions done by the trustees or the employees or directors of the asset management company or the trustee company in the investee companies shall be disclosed by them to the compliance officer within one month of the transaction.
2. The compliance officer shall make a report thereon from the view point of possible conflict of interest and shall submit it to the trustees with his recommendations, if any.
3. The persons covered in sub-regulation (1) may obtain the views of the trustees before entering into the transaction in investee companies, by making a suitable request to them.

GOLD EXCHANGE TRADED FUNDS

Gold Exchange Traded Fund scheme shall mean a mutual fund scheme that invests primarily in gold or gold related instruments.

SEBI (Mutual funds) Regulations, 1996 permits Gold Exchange Traded Fund (GETF) to invest primarily in –

- (a) Gold;
- (b) Gold related instruments i.e. such instruments having gold as underlying, as are specified by SEBI from time to time.

A gold exchange traded fund scheme is subject to the following investment restrictions:

- (a) the funds of any such scheme should be invested only in gold or gold related instruments in accordance

with its investment objective, except to the extent necessary to meet the liquidity requirements for honouring repurchases or redemptions, as disclosed in the offer document; and

- (b) pending deployment of funds in accordance with clause (a), the mutual fund may invest such funds in short term deposits of scheduled commercial banks.

Gold Monetisation Scheme (GMS)

SEBI has designated Gold Monetisation Scheme (GMS) of as a gold related instrument. Investment in GMS of banks by Gold ETFs of mutual funds will be subject to following conditions:

- (a) The cumulative investment by Gold ETF in Gold Deposit Scheme (GDS) and GMS will not exceed 20% of total AUM of such schemes.
- (b) All other conditions applicable to investments in GDS of Banks will also be applicable to investment by Gold ETFs in GMS. Existing investments by Gold ETFs of Mutual Funds under the GDS will be allowed to till maturity under these are withdrawn permanently.

1. Valuation

Since physical gold and other permitted instruments linked to gold are denominated in gold tonnage, it will be valued based on the market price of gold in the domestic market and will be marked to market on a daily basis. The market price of gold in the domestic market on any business day would be arrived at as under:

Domestic price of gold = (London Bullion Market Association AM fixing in US\$/ounce X conversion factor for converting ounce into kg for 0.995 fineness X rate for US\$ into INR) + custom duty for import of gold + sales tax/ octroi and other levies applicable.

The trustees reserve the right to change the source (centre) for determining the exchange rate. The AMC should record in writing the reason for change in the source for determining the exchange rate.

2. Determination of Net Asset Value

NAV of units under the scheme would be calculated as shown below:

$$\text{NAV (₹)} = \frac{\text{Market or Fair Value of Scheme's investments + Current Assets} - \text{Current Liabilities and Provision}}{\text{No. of Units outstanding under Scheme on the Valuation Date}}$$

The NAV shall be calculated up to four decimals.

3. Recurring Expenses

For a GETF, the limits applicable to equity schemes as specified in SEBI Regulations shall be applicable.

4. Benchmark for GETF

As there are no indices catering to the gold sector/securities GETF shall be benchmarked against the price of Gold.

5. Half Yearly Report by Trustees

Physical verification of gold underlying the Gold ETF Units shall be carried out by statutory auditors of mutual fund schemes and reported to trustees on half yearly basis. The confirmation on physical verification of gold shall form part of half yearly report by trustees to SEBI.

REAL ESTATE MUTUAL FUND SCHEMES (REMFS)

“Real Estate Mutual Fund Scheme” means a mutual fund scheme that invests directly or indirectly in real estate assets or other permissible assets in accordance with SEBI (Mutual Funds) Regulations, 1996.

“Real estate assets” means an identifiable immovable property-

- (i) which is located within India in such city as may be specified by SEBI from time to time or in a special economic zone within the meaning of section 2 of the Special Economic Zones Act, 2005;
- (ii) on which construction is complete and which is usable;
- (iii) which is evidenced by valid title documents;
- (iv) which is legally transferable;
- (v) which is free from all encumbrances;
- (vi) which is not subject matter of any litigation;

but does not include –

- I. a project under construction; or
- II. vacant land; or
- III. deserted property; or
- IV. land specified for agricultural use; or
- V. a property which is reserved or attached by any Government or other authority or pursuant to orders of a court of law or the acquisition of which is otherwise prohibited under any law for the time being in force.

SALIENT FEATURES OF REMFS

Some of the salient features of REMFs are as under:

1. An existing Mutual Funds are eligible to launch real estate mutual funds if they have adequate number of experienced key personnel/directors having adequate experience in real estate.
2. Sponsors seeking to set up new Mutual Funds, for launching only real estate mutual fund schemes, shall be carrying on business in real estate for a period not less than five years. They shall also fulfill all other eligibility criteria applicable for sponsoring a MF.
3. Every real estate mutual fund scheme shall be close-ended and its units shall be listed on a recognized stock exchange.
4. Net asset value (NAV) of the scheme shall be declared daily.
5. At least 35% of the net assets of the scheme shall be invested directly in real estate assets. Balance may be invested in mortgage backed securities, securities of companies engaged in dealing in real estate assets or in undertaking real estate development projects and other securities. Taken together, investments in real estate assets, real estate related securities (including mortgage backed securities) shall not be less than 75% of the net assets of the scheme.
6. Unless, otherwise disclosed in the offer document, no mutual fund shall, under all its real estate mutual fund schemes, invest more than thirty percent of its net assets in a single city.
7. Unless otherwise stated, the investment restrictions specified in the Seventh Scheme shall apply.
8. No mutual fund shall transfer real estate assets amongst its schemes.
9. No mutual fund shall invest in any real estate asset which was owned by the sponsor or the asset

management company or any of its associates during the period of last five years or in which the sponsor or the asset management company or any of its associates hold tenancy or lease rights.

10. A real estate mutual fund scheme shall not undertake lending or housing finance activities.

COMPLIANCES UNDER SEBI (LISTING OBLIGATION AND DISCLOSURE REQUIREMENTS) REGULATIONS, 2015

Obligations of Listed Entity which has listed its Mutual Fund Units

Applicability

As per regulation 88(1), the provisions of chapter IX of SEBI (LODR) Regulations, 2015 shall apply to the asset management company managing the mutual fund scheme whose units are listed on the recognised stock exchange(s).

Notwithstanding anything contained in this chapter, the provisions of the Securities and Exchange Board of India (Mutual Funds) Regulations, 1996 and directions issued thereunder shall apply on the listed entity and to the schemes whose units are listed on the recognised stock exchange(s).

Submission of Documents

As per regulation 90(1) states that the listed entity shall intimate to the recognised stock exchange(s), the information relating to daily Net Asset Value, monthly portfolio, half yearly portfolio of those schemes whose units are listed on the recognised stock exchange(s) in the format as specified under SEBI (Mutual Funds) Regulations, 1996 and directions issued there under.

Regulation 90(2) states that the listed entity shall intimate to the recognised stock exchange(s) in the manner specified by the recognized stock exchange(s) of:

- (a) movement in unit capital of those schemes whose units are listed on the recognised stock exchange(s);
- (b) rating of the scheme whose units are listed on the recognised stockexchange(s) and any changes in the rating thereof (wherever applicable);
- (c) imposition of penalties and material litigations against the listed entity and Mutual Fund;
- (d) any prohibitory orders restraining the listed entity from transferring units registered in the name of the unit holders.

Dissemination on the website of stock exchange(s)

Regulation 91 provides that the listed entity shall submit such information and documents, which are required to be disseminated on the listed entity's website in terms of SEBI (Mutual Funds) Regulations, 1996 and directions issued thereunder, to the recognized stock exchange for dissemination.

LESSON ROUND UP

- Mutual Funds, pool their marginal resources, invest in securities and distribute the returns therefrom among them on cooperative principles.
- As in mature markets, mutual funds in emerging markets have been among the fastest growing institutional investors.
- Mutual funds are regulated by SEBI (Mutual Fund) Regulations, 1996
- An investor can subscribe to New fund offers of mutual fund schemes through Application Supported by Block Amount Facility.

- Offer document of mutual funds scheme offering new fund has two parts: Scheme Information Document (SID) and Statement of Additional Information (SAI).
- Various schemes of Mutual Funds are Open ended mutual funds; Close ended mutual funds; Capital Oriented Protection Scheme; Income Oriented Schemes; Growth Oriented Schemes; Hybrid Schemes; High Growth Schemes; Money Market Mutual Funds; Tax Saving Schemes etc.
- Various risks involved in mutual funds are Excessive diversification of portfolio; Losing focus on the securities of the key segments; Too much concentration on blue-chip securities; Poor planning of investment with minimum returns; Unresearched forecast on income, Profits and Government policies etc.
- The provisions of chapter VI B of SEBI (Mutual Funds) Regulation, 1996 shall apply to infrastructure debt fund schemes launched by mutual funds.
- Gold Exchange Traded Fund (GETF) schemes are permitted to invest primarily in
 - (a) Gold.
 - (b) Gold related instruments i.e. such instruments having gold as underlying, as are specified by SEBI from time to time
- Existing Mutual Funds are eligible to launch real estate mutual funds if they have adequate number of experienced key personnel/directors.
- For Listing of Units on stock exchange in addition to SEBI (Mutual Funds) Regulations, 1996, SEBI (Listing Obligations and Disclosure Requirements, 2015 is applicable.

GLOSSARY

Mezzanine Financing	A hybrid of debt and equity financing that is typically used to finance the expansion of existing companies. Mezzanine financing is basically debt capital that gives the lender the rights to convert to an ownership or equity interest in the company if the loan is not paid back in time and in full. It is generally subordinated to debt provided by senior lenders such as banks and venture capital companies.
Parent company of the sponsor	It shall mean a company which holds at least 75% of paid up equity share capital of the sponsor.
New Fund offer	A security offering in which investors may purchase units of a closed-end mutual fund. A new fund offer occurs when a mutual fund is launched, allowing the firm to raise capital for purchasing securities.
Expected Return	The return an investor might expect on an investment if the same investment were made many times over an extended period. The return is found through the use of mathematical analysis.
Investment Objective	The goal that an investor and mutual fund pursue together, e.g. current income, long term capital growth etc.

SELF TEST QUESTIONS

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation.)

1. Discuss the various advantages, schemes and general obligations of Mutual Funds.
2. Describe various schemes of Mutual funds.

[illegible]

Lesson 8

Alternative Investment Fund

LESSON OUTLINE

- Introduction
- Existing Venture Capital Funds
- SEBI (Alternative Investment Funds) Regulations, 2012
- Key Features of AIF Categories
- Placement Memorandum
- Listing
- Transparency
- General Obligations
- Obligations of Manager
- Maintenance of Records
- Winding up
- Guidelines on disclosures, reporting and clarification under AIF Regulations
- Overseas Investment by AIFs
- SEBI (Foreign Venture Capital Investors) Regulations, 2000
- LESSON ROUND UP
- GLOSSARY
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

SEBI had earlier framed the SEBI (Venture Capital Funds) Regulations, 1996 (“VCF Regulations”) to encourage investments into start-ups and mid-size companies. Since the introduction of the VCF Regulations, it was observed by SEBI that the venture capital route was being used by several other categories of funds also such as private equity funds, real estate funds etc. Accordingly, SEBI notified the Alternative Investment Fund (AIF) Regulations, 2012 to govern unregulated entities and create a level playing ground for existing venture capital investors.

Keeping this in view, this lesson is designed to enable the students to have the basic understanding of the Alternative Investment Fund, Regulatory Framework governing AIF in India, Angel Fund and Scheme of angle fund, their working mechanism, types of AIF, their winding up etc. Further the student will also have the overview of Foreign Venture Capital Investors Regulations.

INTRODUCTION

SEBI had earlier framed the SEBI (Venture Capital Funds) Regulations, 1996 ("VCF Regulations") to encourage investments into start-ups and mid-size companies. Since the introduction of the VCF Regulations, it was observed by SEBI that the venture capital route was being used by several other categories of funds such as private equity funds, real estate funds etc. Further since registration as a venture capital fund ("VCF") was not mandatory under the VCF Regulations, not all private equity or other categories of funds were registering with the SEBI. While these funds did not enjoy certain exemptions that were available to VCFs, they were not subjected to any investment restrictions either.

Currently, while retail investors such as mutual funds and collective investment schemes are well regulated, SEBI noted the need for comprehensive regulations to deal with investments that are sourced from diverse parts of the private pool of capital.

Accordingly, SEBI notified the Alternative Investment Fund (AIF) Regulations to govern unregulated entities and create a level playing ground for existing venture capital investors.

The AIF Regulations aim to regulate funds involved in the pooling or raising of private capital from institutional investors or high net worth investors ("HNI") with a view to invest such funds in accordance with a defined investment policy for benefit of the investors and the manager of such fund, irrespective of their legal domicile. These regulations provide that an entity, seeking to pool and manage such private pool of capital for investing in securities or acting as an Alternative Investment Fund ("AIF"), should be registered with the SEBI under these regulations.

EXISTING VENTURE CAPITAL FUNDS

Existing VCFs will be permitted to continue and shall be governed by the VCF Regulations till such fund or scheme managed by the fund is wound up. VCFs will not be permitted to raise any fresh funds after notification of these regulations, as aforesaid, except for commitments already made by investors as on the date of the notification. These VCFs may seek re-registration under AIF Regulations, subject to approval of two-thirds of their investors by value. Existing funds (falling within the definition of an AIF) not registered with SEBI may continue to operate for 6 months from the date of commencement of the AIF Regulations or if it has already made an application for registration under these regulations within those 6 months then till the disposal of its application (extendable up to 12 months in special cases with the permission of SEBI). These funds will not be allowed to float any new scheme without registration under the AIF Regulations. Schemes floated by such funds before coming into force of AIF Regulations, shall only be allowed to continue till maturity. Further existing funds that are currently not registered with SEBI but wish to seek registration under the AIF Regulations may apply to SEBI for exemption from the strict compliance with the AIF Regulations if they are not able to comply with all provisions of these regulations.

SEBI (ALTERNATIVE INVESTMENT FUNDS) REGULATIONS, 2012

The Securities and Exchange Board of India ("SEBI") has notified the SEBI (Alternative Investment Funds) Regulations, 2012 on 21 May, 2012 - a comprehensive regulatory framework for regulating private pools of capital or Alternative Investment Funds, thus bringing various funds investing in Indian securities under a unified regulatory umbrella.

REPEAL OF THE SEBI (VENTURE CAPITAL FUNDS) REGULATIONS, 1996

This Regulation has replaced the existing SEBI (Venture Capital Funds) Regulations, 1996 ("VCF Regulations"). Funds registered under the VCF Regulations shall continue to be regulated by the said regulations till the existing fund or scheme is wound up.

IMPORTANT DEFINITIONS**Alternative Investment Fund**

AIF means any fund established in India in the form of a trust, company, limited liability partnership or a body corporate which:-

- (i) is a privately pooled investment vehicle that collects funds from investors, whether Indian or foreign, for investing it in accordance with a defined investment policy for the benefit of its investors; and
- (ii) is not covered under the SEBI (Mutual Funds) Regulations, 1996, SEBI (Collective Investment Schemes) Regulations, 1999 or any other regulations of SEBI, which aims to regulate fund management activities.

The following are specifically excluded from the purview of AIF Regulations (subject to conditions in certain cases):

- Family Trusts;
- ESOP Trusts;
- Employee Welfare Trusts;
- Holding Companies within the meaning of section 2(46) of Companies Act, 2013;
- Other Special Purpose Vehicles not established by fund managers, including securitization trusts, regulated under a specific regulatory framework;
- Funds managed by registered securitization company or reconstruction company; and
- Any such pool of funds which is directly regulated by any other Indian regulator.

Angel Fund

Angel fund means a sub-category of Venture Capital Fund under Category I- Alternative Investment Fund that raises funds from angel investors and invests in accordance with the provisions of Chapter III-A of these regulations.

Company with family connection

Company with family connection means:

- (a) if the angel investor is an individual,
 - (i) any company which is promoted by such an individual or his relative; or
 - (ii) any company where the individual or his relative is a director; or
 - (iii) any company where the person or his relative has control, or shares or voting rights which entitle them to fifteen percent or more of the shares or voting rights in the company.

Explanation I: For the purpose of this clause, “relative” means a person as defined under section 2 (77) of the Companies Act, 2013.

Explanation II: For the purpose of this clause, “control” shall have the same meaning as assigned to it under sub-regulation (1) of regulation 2 of SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011.

- (b) if the angel investor is a body corporate,
 - (i) any company which is a subsidiary or a holding company of the investor; or
 - (ii) any company which is part of the same group or under the same management of the investor; or

Explanation: For the purpose of this clause, “part of the same group” and “under the same management” shall have the same meaning as assigned to it under regulation 23 of SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009.

- (iii) any company where the body corporate or its directors/partners have control, or shares or voting rights which entitle them to fifteen percent or more of the shares or voting rights in the company.

Debt Funds

These funds will primarily make investments in debt or debt securities of listed or unlisted investee companies.

Hedge Funds

Hedge Funds will employ diverse or complex trading strategies and invests and trades in securities having diverse risks or complex products, including listed and unlisted derivatives.

Infrastructure Funds

These funds will primarily invest in unlisted securities or partnership interest or listed debt or securitized debt instruments of investee companies or special purpose vehicles engaged in or formed for, the purpose of operating or holding infrastructure projects.

Investible Fund

It means corpus of the Alternative Investment Fund net of estimated expenditure for administration and management of the fund.

Private Equity (“PE”) Funds

PE funds will invest primarily in equity or equity linked instruments or partnership interests of investee companies.

Small and Medium Enterprises (“SME”) Funds

These funds will invest primarily in unlisted securities of investee companies which are SMEs or securities of those SMEs which are listed or proposed to be listed on a SME exchange or SME segment of an exchange.

Social Venture Funds

These funds will invest primarily in securities or units of social ventures and which satisfy social performance norms laid down by the fund and whose investors may agree to receive restricted or muted returns.

Sponsor

It means any person or persons who set up the Alternative Investment Fund and includes promoter in case of a company and designated partner in case of a limited liability partnership.

Venture Capital Funds

These funds will primarily invest in unlisted securities of start ups, emerging or early stage venture capital undertakings mainly involved in new products, new services, technology or intellectual property rights based activities or a new business model and shall include an angel fund as defined under Chapter III-A

Venture Capital Undertaking

“venture capital undertaking” means a domestic company:

- (i) which is not listed on a recognised stock exchange in India at the time of making investment; and
- (ii) which is engaged in the business for providing services, production or manufacture of article or things and does not include following activities or sectors:
 - (1) non-banking financial companies;

- (2) gold financing;
- (3) activities not permitted under industrial policy of Government of India;
- (4) any other activity which may be specified by SEBI in consultation with Government of India from time to time.

CATEGORIES OF AIF

SEBI has classified AIF into the following three broad categories:

Category I: - Fund that invest in start-up or early stage ventures or social ventures or Small and Medium Enterprises (SMEs) or infrastructure or other sectors which the government or regulators consider as socially or economically desirable which include VCF, SME Funds, Social Venture Funds (SVF), Infra Funds and such other AIFs as may be specified in the AIF Regulations.

Category II: - Funds that do not fall in Category I and III AIF and those that do not undertake leverage or borrowing other than to meet the permitted day to day operational requirement including Private Equity Funds or Debt Funds.

Category III: - Funds that employ diverse or complex trading strategies and may employ leverage including through investment in listed or unlisted derivatives, for e.g. Hedge Funds.

SEBI has allowed the Category - III Alternative Investment Funds (AIFs) to participate in the commodity derivatives market.

REGISTRATION OF AIF

- All AIFs are required to be mandatorily registered under any one of the above mentioned categories.
- AIF Regulations permit launch of multiple schemes under an AIF without separate registration from SEBI subject to filing of Information Memorandum with SEBI.
- The certificate of registration, once granted, shall be valid till the concerned AIF is wound up.

CHANGE IN CATEGORY OF THE ALTERNATIVE INVESTMENT FUND (AIF)

SEBI has issued guidelines for alternative investment funds (AIFs) to change their registration categories based on risk exposure. These guidelines describe the rules and procedure regarding changes from one category of AIF registration to another. Regulation 7(2) of AIF Regulations specified that an AIF which has been granted registration under a particular category cannot change its category subsequent to registration, except with the approval of SEBI.

- Only AIFs that have not made any investments under their existing category would be allowed to apply for changing their classification.
- Any AIF proposing to change its category is required to make an application to the SEBI for the same along with the application fees of Rs. 1 lakh. Additionally, they need to intimate the rationale for the proposed change.
- In case the AIF has raised funds prior to the application for change in category, the AIF would be required to inform all its investors providing them the option to withdraw their funds garnered without any penalties. Any fees collected from investors seeking to withdraw commitments/funds shall be returned to them. Partial withdrawal may be allowed subject to compliance with the minimum investment amount required under the AIF Regulations.
- The AIF would not make any investments other than in liquid funds/banks deposits until approval for the change in category is granted by the SEBI.

- On approval of the request from SEBI, the AIF shall send a copy of the revised placement memorandum and other relevant information to all its investors.

INVESTMENT STRATEGY

All Alternative Investment Funds shall state investment strategy, investment purpose and its investment methodology in its placement memorandum to the investors.

Any material alteration to the fund strategy shall be made with the consent of atleast two-thirds of unit holders by value of their investment in the Alternative Investment Fund.

INVESTMENT IN ALTERNATIVE INVESTMENT FUND

Investment in all categories of Alternative Investment Funds shall be subject to the following conditions:-

- (a) the Alternative Investment Fund may raise funds from any investor whether Indian, foreign or non-resident Indians by way of issue of units;
- (b) each scheme of the Alternative Investment Fund shall have corpus of atleast twenty crore rupees;
- (c) the Alternative Investment Fund shall not accept from an investor, an investment of value less than one crore rupees. However, in case of investors who are employees or directors of the Alternative Investment Fund or employees or directors of the Manager, the minimum value of investment shall be 25 lakh rupees.
- (d) the Manager or Sponsor shall have a continuing interest in the Alternative Investment Fund of not less than two and half percent of the corpus or 5 crore rupees, whichever is lower, in the form of investment in the Alternative Investment Fund and such interest shall not be through the waiver of management fees.

However, for Category III Alternative Investment Fund, the continuing interest shall be not less than five percent of the corpus or ten crore rupees, whichever is lower.

- (e) the Manager or Sponsor shall disclose their investment in the Alternative Investment Fund to the investors of the Alternative Investment Fund;
- (f) no scheme of the Alternative Investment Fund shall have more than 1000 investors;

However, the provisions of Companies Act, 2013 shall apply to the Alternative Investment Fund, if it is formed as a company.

- (g) the fund shall not solicit or collect funds except by way of private placement.

INVESTMENT IN ANGEL FUNDS

Angel funds shall only raise funds by way of issue of units to angel investors. An angel fund shall have a corpus of at least ten crore rupees. Angel funds shall accept, up to a maximum period of three years, an investment of not less than twenty five lakh rupees from an angel investor. An angel fund may also invest in the securities of companies incorporated outside India subject to such conditions or guidelines that may be stipulated or issued by the RBI and SEBI from time to time.

INVESTMENT BY ANGEL FUNDS

Angel funds shall invest in venture capital undertakings which :

- (a) Complies with the criteria regarding the age of the venture capital undertaking/statup issued by the Department of Industrial Policy and Promotion under the Ministry of Commerce and Industry and such other Policy made in this regard which may be in force;
- (b) Have a turnover of less than twenty five crore rupees;

- (c) Are not promoted or sponsored by or related to an industrial group whose group turnover exceeds three hundred crore rupees; and

Explanation I: For the purpose of this clause, “industrial group” shall include a group of body corporates with the same promoter(s)/promoter group, a parent company and its subsidiaries, a group of body corporates in which the same person/ group of persons exercise control, and a group of body corporates comprised of associates/subsidiaries/holding companies.

Explanation II: For the purpose of this clause, “group turnover” shall mean combined total revenue of the industrial group.

- (d) Are not companies with family connection with any of the angel investors who are investing in the company;
- (e) Investment by an angel fund in any venture capital undertaking shall not be less than fifty lakh rupees and shall not exceed five crore rupees;
- (f) Investment by an angel fund in the venture capital undertaking shall be locked-in for a period of three years;
- (g) Angel funds shall not invest in associates;
- (h) Angel funds shall not invest more than twenty-five per cent of the total investments under all its schemes in one venture capital undertaking;
- (i) An angel funds may also invest in the securities of companies incorporated outside India subject to such conditions or guidelines that may be stipulated or issued by RBI and SEBI from time to time.

GENERAL INVESTMENT CONDITIONS AND RESTRICTIONS

Investments by all categories of Alternative Investment Funds shall be subject to the following conditions:-

- (a) Alternative Investment Fund may invest in securities of companies incorporated outside India subject to such conditions or guidelines that may be stipulated or issued by the Reserve Bank of India and SEBI from time to time;
- (b) Co-investment in an investee company by a Manager or Sponsor shall not be on terms more favourable than those offered to the Alternative Investment Fund;
- (c) Category I and II Alternative Investment Funds shall invest not more than twenty five percent of the investible funds in one Investee Company;
- (d) Category III Alternative Investment Fund shall invest not more than ten percent of the investible funds in one Investee Company;
- (e) Alternative Investment Fund shall not invest in associates except with the approval of seventy five percent of investors by value of their investment in the Alternative Investment Fund;
- (f) Un-invested portion of the investible funds may be invested in liquid mutual funds or bank deposits or other liquid assets of higher quality such as Treasury bills, CBLOs, Commercial Papers, Certificates of Deposits, etc. till deployment of funds as per the investment objective;
- (g) Alternative Investment Fund may act as Nominated Investor as specified in SEBI (ICDR) Regulations, 2009.

KEY FEATURES OF AIF CATEGORIES

Category I		Category II	Category III
<ul style="list-style-type: none">• Minimum tenure of 3 year• Close ended fund• The tenure may be extended for a further period of 2 years only with the approval of two-third of the the unit holders by value of their investment.			<ul style="list-style-type: none">• No minimum tenure prescribed.• Open-ended or close ended fund.• The tenure may be extended for a further period of 2 years in case of close-ended fund subject to approval of two-third of the the unitholders by value of their investment.
Leverage / Hedging			
<ul style="list-style-type: none">• Shall not borrow/leverage except for meeting temporary funding requirements, which shall not exceed 30 days.• The borrowing cannot be on more than four occasions in a year and cannot exceed 10% of the investible funds.	<ul style="list-style-type: none">• Shall not borrow/leverage except for meeting temporary funding requirements,which shall not exceed 30 days.• The borrowing cannot be on more than four occasions in a year and cannot exceed 10% of the investible funds.• Funds may engage in hedging subject to guidelines as specified by SEBI.	<ul style="list-style-type: none">• May leverage or borrow (Subject to consent from investors and maximum limit specified by SEBI)	
Investment in one investor company			
<ul style="list-style-type: none">• Shall not invest more than 25% of its investible funds in one investee company		<ul style="list-style-type: none">• Maximum 10% of the investible funds in one investee company	
Tax “Pass Through”			
<ul style="list-style-type: none">• Category I AIFs will be considered as venture capital funds/companies for the purpose of Section 10(23FB) of the Income Tax Act, 1961	<ul style="list-style-type: none">• The income from Category II and III funds will not be exempt under section 10(23FB) of the Income Tax Act, 1961• Taxation of such hands would depend on the legal status of the fund i.e. company limited liability partnership or trust.		
Valuation			
<ul style="list-style-type: none">• AIF must disclose to the investors the valuation procedure and the methodology for valuing assets.• Valuation should be carried out by an independent valuers once in every 6 months. This period can be extended to one year with the approval of 75% of the investors by value.		<ul style="list-style-type: none">• AIF must disclose the valuation procedure and the methodology for valuing assets.• AIF to ensure that calculation of net asset value is independent from the fund management function of the AIF; NAV to be disclosed to investors as per the regulations.	

Reporting

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| <ul style="list-style-type: none"> • Within 180 days from the end of the year, an annual report is required to be presented to the investor. | <ul style="list-style-type: none"> • Within 180 days from the end of the year an annual report is required to be presented to the investors; • Within 60 days from the end of the quarter, AIF is also required to provide a quarterly report to the investors. |
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PLACEMENT MEMORANDUM

Alternative Investment Fund and Angel Fund shall raise funds through private placement by issue of information memorandum or placement memorandum, by whatever name called.

Such information memorandum or placement memorandum must contain all material information about the Alternative Investment Fund and the Manager, background of key investment team of the Manager, targeted investors, fees and all other expenses proposed to be charged, tenure of the Alternative Investment Fund or scheme, conditions or limits on redemption, investment strategy, risk management tools and parameters employed, key service providers, conflict of interest and procedures to identify and address them, disciplinary history, the terms and conditions on which the Manager offers investment services, its affiliations with other intermediaries, manner of winding up of the Alternative Investment Fund or the scheme and such other information as may be necessary for the investor to take an informed decision on whether to invest in the Alternative Investment Fund.

SCHEMES

Schemes may be launch subject to filing of a scheme memorandum atleast thirty days in case of Alternative Investment Funds and atleast ten working days in case of Angel fund prior to launch of scheme with SEBI. Such scheme memorandum shall contain all material information about the investments proposed under such scheme. No scheme of the angel fund shall have more than two hundred angel investors.

LISTING

Units of close ended Alternative Investment Fund may be listed on stock exchange subject to a minimum tradable lot of one crore rupees. Listing of Alternative Investment Fund units shall be permitted only after final close of the fund or scheme. Units of angel funds shall not be listed on any recognised stock exchange.

TRANSPARENCY

All Alternative Investment Funds shall ensure transparency and disclosure of information to investors on the following:

- financial, risk management, operational, portfolio, and transactional information regarding fund investments shall be disclosed periodically to the investors;
- any fees prescribed to the Manager or Sponsor; and any fees charged to the Alternative Investment Fund or any investee company by an associate of the Manager or Sponsor shall be disclosed periodically to the investors;
- any inquiries/ legal actions by legal or regulatory bodies in any jurisdiction, as and when occurred;
- any material liability arising during the Alternative Investment Fund's tenure shall be disclosed, as and when occurred;
- any breach of a provision of the placement memorandum or agreement made with the investor or any other fund documents, if any, as and when occurred;
- change in control of the Sponsor or Manager or Investee Company;

- (g) Alternative Investment Fund shall provide at least on an annual basis, within 180 days from the year end, reports to investors including the following information, as may be applicable to the Alternative Investment Fund:-
 - A. financial information of investee companies.
 - B. material risks and how they are managed which may include:
 - (i) concentration risk at fund level;
 - (ii) foreign exchange risk at fund level;
 - (iii) leverage risk at fund and investee company levels;
 - (iv) realization risk (i.e. change in exit environment) at fund and investee company levels;
 - (v) strategy risk (i.e. change in or divergence from business strategy) at investee company level;
 - (vi) reputation risk at investee company level;
 - (vii) extra-financial risks, including environmental, social and corporate governance risks, at fund and investee company level.
- (h) Category III Alternative Investment Fund shall provide quarterly reports to investors in respect of clause (g) within 60 days of end of the quarter;
- (i) Any significant change in the key investment team shall be intimated to all investors;
- (j) Alternative Investment Funds shall provide, when required by SEBI, information for systemic risk purposes (including the identification, analysis and mitigation of systemic risks).

GENERAL OBLIGATIONS

- (1) All Alternative Investment Funds shall review policies and procedures, and their implementation, on a regular basis, or as a result of business developments, to ensure their continued appropriateness.
- (2) The Sponsor or Manager of Alternative Investment Fund shall appoint a custodian registered with SEBI for safekeeping of securities if the corpus of the Alternative Investment Fund is more than 500 crore rupees. However, the Sponsor or Manager of a Category III Alternative Investment Fund shall appoint such custodian irrespective of the size of corpus of the Alternative Investment Fund.
- (3) All Alternative Investment Funds shall inform SEBI in case of any change in the Sponsor, Manager or designated partners or any other material change from the information provided by the Alternative Investment Fund at the time of application for registration.
- (4) In case of change in control of the Alternative Investment Fund, Sponsor or Manager, prior approval from SEBI shall be taken by the Alternative Investment Fund.
- (5) The books of accounts of the Alternative Investment Fund shall be audited annually by a qualified auditor.
- (6) The Manager shall be obliged to address all investor complaints, provide to SEBI any information sought by SEBI, maintain all records as may be specified by SEBI, take all steps to address conflict of interest as specified in these regulations, and ensure transparency and disclosure as specified in the regulations.

MAINTENANCE OF RECORDS

The Manager or Sponsor shall be required to maintain following records describing:

- (a) the assets under the scheme/fund;
- (b) valuation policies and practices;
- (c) investment strategies;

- (d) particulars of investors and their contribution;
- (e) rationale for investments made.

The records shall be maintained for a period of five years after the winding up of the fund.

WINDING UP

- (1) An Alternative Investment Fund set up as a trust shall be wound up:
 - (a) when the tenure of the Alternative Investment Fund or all schemes launched by the Alternative Investment Fund, as mentioned in the placement memorandum is over; or
 - (b) if it is the opinion of the trustees or the trustee company, as the case may be, that the Alternative Investment Fund be wound up in the interests of investors in the units; or
 - (c) if seventy five percent of the investors by value of their investment in the Alternative Investment Fund pass a resolution at a meeting of unit holders that the Alternative Investment Fund shall be wound up; or
 - (d) if SEBI so directs in the interests of investors.
- (2) An Alternative Investment Fund set up as a limited liability partnership shall be wound up in accordance with the provisions of the Limited Liability Partnership Act, 2008:
- (3) An Alternative Investment Fund set up as a company shall be wound up in accordance with the provisions of the Companies Act, 2013.
- (4) An Alternative Investment Fund set up as a body corporate shall be wound up in accordance with the provisions of the statute under which it is constituted.
- (5) The trustees or trustee company or the Board of Directors or designated partners of the Alternative Investment Fund, as the case maybe, shall intimate SEBI and investors of the circumstances leading to the winding up of the Alternative Investment Fund.
- (6) On and from the date of intimation, no further investments shall be made on behalf of the Alternative Investment Fund so wound up.
- (7) Within one year from the date of intimation, the assets shall be liquidated, and the proceeds accruing to investors in the Alternative Investment Fund shall be distributed to them after satisfying all liabilities.
- (8) Subject to the conditions, if any, contained in the placement memorandum or contribution agreement or subscription agreement, as the case may be, in specific distribution of assets of the Alternative Investment Fund, shall be made by the Alternative Investment Fund at any time, including on winding up, as per the preference of investors, after obtaining approval of at least 75 % of the investors by value of their investment in the Alternative Investment Fund.
- (9) Upon winding up of the Alternative Investment Fund, the certificate of registration shall be surrendered to SEBI.

GUIDELINES ON DISCLOSURES, REPORTING AND CLARIFICATIONS UNDER AIF REGULATIONS

SEBI has provided certain clarifications on the AIF Regulations in order to increase transparency to the investors by issuing guidelines on this behalf.

SEBI has prescribed that Category III AIFs should report to the custodian the amount of leverage at the end of the day (based on closing prices) by the end of next working day.

SEBI has further clarified that AIFs should include in the placement memorandum detailed disclosures of the fees and charges as applicable to the investors and disciplinary history of the AIFs, sponsors, managers, their Directors/partners/ promoters and associates etc.

In case of changes to the placement memorandum which significantly influences the decision of the investor to continue to be invested in the AIF, the following process should be followed by the AIF:

- (1) Existing unit holders who do not wish to continue after the change should be provided an exit option.
- (2) If the scheme of the AIF is open ended, the exit option can be provided by either of the following:
 - Buying out of units of the dissenting investors by the manger/ someone else arranged by the manager, valuation of which should be based on market price of underlying assets.
 - Redemption of units of the investors through sale of underlying assets.
- (3) If the scheme of the AIF is close ended, the exit option can be provided as follows :
 - Buying out of units of the dissenting investors by the manger/ someone else arranged by the manager.
 - Prior to buying out of such units, valuation of those units should be undertaken by 2 independent valuers and exit should be at a value at least as large as average of the two valuations.
 - The trustee of AIF (in case AIF is a trust) or sponsor (in case of any other AIF) should be responsible for overseeing the process.

Moreover, all guidelines that are issued by SEBI with respect to KYC requirements, Anti-Money Laundering and outsourcing of activities should be applicable to AIFs and the manager of the AIF should be responsible for complying with such guidelines.

OVERSEAS INVESTMENT BY ALTERNATIVE INVESTMENT FUNDS

Under Regulation 15(1)(a) of AIF Regulations, “Alternative Investment Fund may invest in securities of companies incorporated outside India subject to such conditions or guidelines that may be stipulated or issued by the Reserve Bank of India and SEBI from time to time.”

In this regard, Reserve Bank of India (RBI) vide its Circular No.48 dated December 09, 2014 has permitted an Alternative Investment Fund (AIF), registered with SEBI, to invest overseas in terms of the provisions issued under the A.P. (DIR Series) Circulars No. 49 and 50 dated April 30, 2007 and May 04, 2007 respectively.

In accordance with the aforesaid RBI circular, it is stated as under:

- AIFs may invest in equity and equity linked instruments only of offshore venture capital undertakings, subject to overall limit of USD 500 million (combined limit for AIFs and Venture Capital Funds registered under the SEBI (Venture Capital Funds) Regulations, 1996).
- AIFs desirous of making investments in offshore venture capital undertakings shall submit their proposal for investment (in the attached format at Annexure) to SEBI for prior approval. It is clarified that no separate permission from RBI is necessary in this regard.
- For the purpose of such investment, it is clarified that “Offshore Venture Capital Undertakings” means a foreign company whose shares are not listed on any of the recognized stock exchange in India or abroad.
- Investments would be made only in those companies which have an Indian connection (e.g. company which has a front office overseas, while back office operations are in India).
- Such investments shall not exceed 25% of the investible funds of the scheme of the AIF.
- The allocation of investment limits would be done on ‘first come first serve’ basis, depending on the availability in the overall limit of USD 500 million.
- In case an AIF who is allocated certain investment limit, wishes to apply for allocation of further investment limit, the fresh application shall be dealt with on the basis of the date of its receipt and no preference

shall be granted to it in fresh allocation of investment limit.

- The AIF shall have a time limit of 6 months from the date of approval from SEBI for making allocated investments in offshore venture capital undertakings. In case the applicant does not utilize the limits allocated within the stipulated period, SEBI may allocate such unutilized limit to other applicants.
- These investments would be subject to Notification No. FEMA120/RB-2004 dated July 7, 2004 [Foreign Exchange Management (Transfer or Issue of Any Foreign Security) Regulations, 2004] including amendments thereof and related directions issued by RBI from time to time.
- AIFs shall not invest in Joint venture/Wholly Owned Subsidiary while making overseas investments.
- AIFs shall adhere to FEMA Regulations and other guidelines specified by RBI from time to time with respect to any structure which involves Foreign Direct Investment (FDI) under Overseas Direct Investment (ODI) route.
- AIFs shall comply with all requirements under RBI guidelines on opening of branches/subsidiaries/Joint Venture /undertaking investment abroad by NBFCs, where more than 50% of the funds of the AIF has been contributed by a single NBFC.

It is clarified that from the date of this circular, the tenure of any scheme of the AIF shall be calculated from the date of final closing of the scheme.

SEBI (FOREIGN VENTURE CAPITAL INVESTORS) REGULATIONS, 2000

Foreign Venture Capital Investor means an investor incorporated and established outside India, which proposes to make investment in venture capital fund(s) or venture capital undertakings in India and is registered under these Regulations.

APPLICATION FOR GRANT OF CERTIFICATE

The applicant is required to make an application along with the registration fee to SEBI for the purposes of seeking registration in the form specified under these regulations.

ELIGIBILITY CRITERIA

SEBI assesses the application of VCF on the following criteria:

- (i) the applicants track record, professional competence, financial soundness, experience, general reputation of fairness and integrity;
- (ii) whether the applicant has been granted necessary approval by the Reserve Bank of India for making investments in India;
- (iii) whether the applicant is an investment company, investment trust, investment partnership, pension fund, mutual fund, endowment fund, university fund, charitable institution or any other entity incorporated outside India; or
- (iv) whether the applicant is an asset management company, investment manager or investment management company or any other investment vehicle incorporated outside India;
- (v) whether the applicant is authorised to invest in venture capital fund or carry on activity as a foreign venture capital investors or alternative investment fund;
- (vi) whether the applicant is regulated by an appropriate foreign regulatory authority or is an income tax payer; or submits a certificate from its banker of its or its promoter's track record where the applicant is neither a regulated entity nor an income tax payer;

- (vii) the applicant has not been refused a certificate by SEBI;
- (viii) whether the applicant is a fit and proper person.

SEBI may require the applicant to furnish further information, if it considers necessary. An application which is not complete in all respects is rejected by SEBI. However before rejecting any such application, the applicant should be given an opportunity to remove, within thirty days of the date of receipt of communication, the objections indicated by SEBI. SEBI may, on being satisfied that it is necessary to extend the period specified above may extend such period which shall not beyond ninety days.

PROCEDURE FOR GRANT OF CERTIFICATE

If SEBI is satisfied that the applicant is eligible for the grant of certificate, it should send intimation to the applicant and on the receipt of intimation, the applicant has to pay the registration fee specified in these Regulations. SEBI on receipt of the registration fee grants a certificate of registration.

PROCEDURE WHERE CERTIFICATE IS NOT GRANTED

After considering an application, if SEBI is of the opinion that a certificate should not be granted, it may reject the application after giving the applicant a reasonable opportunity of being heard. The decision of SEBI to reject the application should be communicated to the applicant. Any applicant whose application has been rejected should not carry on any activity as a Foreign Venture Capital Investor.

CONDITIONS OF CERTIFICATE

The certificate to be granted to the foreign venture capital is subject to the the conditions that:

- (i) it should abide by the provisions of the Act, and these regulations;
- (ii) it should appoint a domestic custodian for purpose of custody of securities;
- (iii) it should enter into arrangement with a designated bank for the purpose of operating a special non-resident rupee or foreign currency account;
- (iv) it should forthwith inform SEBI in writing if any information or particulars previously submitted to SEBI are found to be false or misleading in any material particular or if there is any change in the information already submitted.

INVESTMENT CRITERIA FOR A FOREIGN VENTURE CAPITAL INVESTOR

All investments to be made by a foreign venture capital investors should be subject to the following conditions:

- (a) it should disclose to SEBI its investment strategy.
- (b) it can invest its total funds committed in one venture capital fund or alternative investment fund.
- (c) it shall make investments as enumerated below:
 - (i) atleast 66.67% of the investible funds should be invested in unlisted equity shares or equity linked instruments of venture capital undertaking or investee company.
 - (ii) not more than 33.33% of the investible funds may be invested by way of:
 - (a) subscription to initial public offer of a venture capital undertaking or investee company whose shares are proposed to be listed;
 - (b) debt or debt instrument of a venture capital undertaking or investee company in which the foreign venture capital investor has already made an investment by way of equity.

- (c) preferential allotment of equity shares of a listed company subject to lock in period of one year.
- (d) Special Purpose Vehicles which are created for the purpose of facilitating or promoting investment in accordance with these Regulations.
- (e) It shall disclose the duration of life cycle of the fund.

The investment conditions and restrictions stipulated, above shall be achieved by the Foreign Venture Capital Investor by the end of its life cycle.

MAINTENANCE OF BOOKS AND RECORDS

Every Foreign Venture Capital Investor is required to maintain for a period of eight years, books of accounts, records and documents which should give a true and fair picture of the state of affairs of the Foreign Venture Capital Investor. Every Foreign Venture Capital Investor should intimate to SEBI, in writing, the place where the books, records and documents are being maintained.

GENERAL OBLIGATIONS AND RESPONSIBILITIES

Foreign Venture Capital Investor or a global custodian acting on behalf of the foreign venture capital investor should enter into an agreement with the domestic custodian to act as a custodian of securities for Foreign Venture Capital Investor. Foreign Venture Capital Investor should ensure that domestic custodian takes steps for monitoring of investment of Foreign Venture Capital Investors in India, furnishing of periodic reports to SEBI and furnishing such information as may be called for by SEBI.

APPOINTMENT OF DESIGNATED BANK

Foreign Venture Capital Investor is required to appoint a branch of a bank approved by Reserve Bank of India as designated bank for opening of foreign currency denominated accounts or special non-resident rupee account.

INSPECTION OR INVESTIGATION

SEBI may, *suo moto* or upon receipt of information or complaint, cause an inspection or investigation to be made in respect of conduct and affairs of any foreign venture capital investor by an Officer whom SEBI considers fit.

ACTION AGAINST INTERMEDIARY

SEBI may initiate action for suspension or cancellation of registration of an intermediary holding a certificate of registration under section 12 of the Act who fails to exercise due diligence in the performance of its functions or fails to comply with its obligations under these regulations.

However, no such certificate of registration shall be suspended or cancelled unless the procedure specified in the regulations applicable to such intermediary is complied with.

APPEAL TO SECURITIES APPELLATE TRIBUNAL (SAT)

Any person aggrieved by an order of SEBI may prefer an appeal to the Securities Appellate Tribunal.

LESSON ROUND UP

- SEBI notified the Alternative Investment Fund (AIF) Regulations to govern unregulated entities and create a level playing ground for existing venture capital investors.
- This Regulation has replaced the existing SEBI (Venture Capital Funds) Regulations, 1996 funds registered under the VCF Regulations shall continue to be regulated by the said regulations till the existing fund or scheme is wound up.
- SEBI has classified AIF into three broad categories i.e Category I, Category II, Category III.
- All AIFs are required to be mandatorily registered under any one of the above mentioned categories.
- Any AIF/scheme shall not have more than 1,000 investors.
- Alternative Investment Fund shall raise funds through private placement by issue of information memorandum or placement memorandum, by whatever name called.
- Listing of Alternative Investment Fund units shall be permitted only after final close of the fund or scheme.
- The records maintained by the Manager/Sponsor is required to be maintained for a period of five years after the winding up of the fund.

GLOSSARY

Corpus	– It means the total amount of funds committed by investors to the Alternative Investment Fund by way of a written contract or any such document as on a particular date.
Investee Company	– It means any company, special purpose vehicle or limited liability partnership or body corporate in which an AIF makes an investment.
Manager	– Manager means any person or entity who is appointed by the Alternative Investment Fund to manage its investments by whatever name called and may also be same as the sponsor of the Fund.
Unit	– Unit means beneficial interest of the investors in the Alternative Investment Fund or a scheme of the Alternative Investment Fund and shall include shares or partnership interests.

SELF TEST QUESTIONS

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation.)

1. What is Alternative Investment Fund?
2. Briefly explain the different categories of Alternative Investment Fund.
3. Write Short notes on the following:
 - (i) Angel Fund
 - (ii) Investible Fund
 - (iii) Social Venture Fund
 - (iv) SME Fund
4. What is placement memorandum? Discuss briefly the contents of placement Memorandum?
5. What are the obligation of the manager under the AIF regulation?
6. What is the procedure for winding up?

Lesson 9

Collective Investment Schemes

LESSON OUTLINE

- Introduction
- SEBI (Collective Investment Schemes) Regulations, 1999 – An Overview
- Application Fee to accompany the Application
- Conditions for Eligibility
- Grant of Certificate
- Terms and Conditions
- Procedure where registration is not granted
- Restriction on Business Activities
- Obligations of Collective Investment Management Company (CIMC)
- Submission of Information and Documents
- Trustees and their Obligations
- Contents of Trust Deed
- Eligibility for Appointment as Trustee
- Rights and obligations of Trustee
- Termination of Trusteeship
- Termination of the Agreement with the CIMC
- Procedure for Launching of Schemes
- Disclosures in the Offer Document
- Allotment of Units and Refunds of Money
- Unit Certificates
- Transfer of Units
- Investments and Segregation of Funds
- Listing of schemes
- Winding up of schemes
- Requirements with respect to the listing of units or any other instrument of a CIS on a recognised stock exchange.
- Penal provisions
- LESSON ROUND UP
- GLOSSARY
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

A collective investment scheme is a trust based scheme that comprises a pool of assets that is managed by a collective investment scheme manager and is governed by the Collective Investment Schemes Regulations notified by SEBI. Collective Investment Schemes (CIS) provide a relatively secure means of investing on the Stock Exchange and other financial instruments. The sum of money that are exchanged on the Stock Exchange and in the money markets make them too pricing for most people. With a CIS, the money or funds from a group of investors are pooled or collected together to form a CIS portfolio.

This lesson gives the student an overview of the Collective Investment Scheme and Collective Investment Management Companies (CIMC) with the features, procedure of registration of such company, responsibilities of CIMC, submission of information and documents by CIMC, content of the offer document etc.

INTRODUCTION

A collective investment scheme is a trust based scheme that comprises a pool of assets that is managed by a collective investment scheme manager and is governed by the Collective Investment Schemes Regulations given by SEBI. Collective Investment Schemes (CIS) are a popular form of investment, and they are accessible to all. Each investor has a proportional stake in the CIS portfolio based on how much money he or she contributed. The word 'unit' refers to the portion or part of the CIS portfolio that is owned by the investor. The 'trust' is the financial instrument that is created in order to manage the investment. The trust enables financial experts to invest the money on behalf of the CIS investor. Collective Investment Schemes provide a relatively secure means of investing on the Stock Exchange, and other financial instruments. The sum of money that are exchanged on the Stock Exchange and in the Money Markets make them too pricey for most people. With a CIS, the money or funds from a group of investors are pooled or collected together to form a CIS portfolio.

In order to strengthen the hands of SEBI to protect interests of investors in plantation companies, the Securities Laws (Amendment) Act, 1999 amended the definition of 'securities' in the SC(R) Act, so as to include within its ambit the units or any other instruments issued by any CIS to the investors in such schemes. The Act also inserted a definition of the CIS in the Securities and Exchange Board of India Act, 1992.

The International Organisation of Securities Commission (IOSCO) in its Report on Investment Management of the Technical Committee defined a Collective Investment Scheme (CIS) as an open ended collective investment scheme that issues redeemable units and invests primarily in transferable securities or money market instruments.

According to SEBI Act, 1992, 'Collective Investment Scheme' means any scheme or arrangement which satisfies the conditions specifies in section 11AA.

Section 11AA provides that any scheme or arrangement which satisfies the conditions referred to in sub-section (2) or sub-section (2A) shall be a collective investment scheme.

However, any pooling of funds under any scheme or arrangement, which is not registered with SEBI or is not covered under sub-section (3), involving a corpus amount of one hundred crore rupees or more shall be deemed to be a collective investment scheme.

Sub-section (2) lays down that any scheme or arrangement made or offered by any person under which,—

- (i) the contributions, or payments made by the investors, by whatever name called, are pooled and utilized for the purposes of the scheme or arrangement;
- (ii) the contributions or payments are made to such scheme or arrangement by the investors with a view to receive profits, income, produce or property, whether movable or immovable, from such scheme or arrangement;
- (iii) the property, contribution or investment forming part of scheme or arrangement, whether identifiable or not, is managed on behalf of the investors;
- (iv) the investors do not have day-to-day control over the management and operation of the scheme or arrangement.

Sub-section 2A provides that any scheme or arrangement made or offered by any person shall satisfy the conditions as may be specified in accordance with the regulations made under this Act.

(3) Notwithstanding anything contained in sub-section (2) or sub-section (2A) any scheme or arrangement –

- (i) made or offered by a co-operative society registered under the Co-operative Societies Act, 1912 or a society being a society registered or deemed to be registered under any law relating to co-operative societies for the time being in force in any State;

- (ii) under which deposits are accepted by non-banking financial companies as defined in clause (f) of section 45-I of the Reserve Bank of India Act, 1934;
- (iii) being a contract of insurance to which the Insurance Act, 1938, applies;
- (iv) providing for any Scheme, Pension Scheme or the Insurance Scheme framed under the Employees Provident Fund and Miscellaneous Provisions Act, 1952;
- (v) under which deposits are accepted under section 74 of the Companies Act, 2013;
- (vi) under which deposits are accepted by a company declared as a Nidhi or a mutual benefit society under section 406 of the Companies Act, 2013;
- (vii) falling within the meaning of Chit business as defined in clause (d) of section 2 of the Chit Fund Act, 1982;
- (viii) under which contributions made are in the nature of subscription to a mutual fund;
- (ix) such other scheme or arrangement which the Central Government may, in consultation with SEBI, notify,

shall not be a collective investment scheme.

SEBI (COLLECTIVE INVESTMENT SCHEMES) REGULATIONS, 1999 – AN OVERVIEW

SEBI (Collective Investment Schemes) Regulations, 1999 defines Collective Investment Management Company means a company incorporated under the Companies Act, 2013 and registered with SEBI under these regulations, whose object is to organize, operate and manage a collective investment.

No person other than a Collective Investment Management Company which has obtained a certificate under the regulations should carry on or sponsor or launch a collective investment scheme. Any person proposing to carry any activity as a Collective Investment Management Company on or after the commencement of the regulations should make an application to SEBI for the grant of registration in the specified form.

“Close ended collective investment scheme” means any collective investment scheme launched by a collective investment management company. In which the maturity period of the collective investment scheme is specified and there is no provision for repurchase before the expiry of the collective investment scheme.

“Collective investment scheme property” includes :

- (i) subscription of money or money's worth (including bank deposits) to the collective investment scheme;
- (ii) property acquired, directly or indirectly, with, or with the proceeds of, subscription of money retired to in item (i); or
- (iii) income arising, directly or indirectly from, subscription money or property retired to in item (i) or (iii).

APPLICATION FEE TO ACCOMPANY THE APPLICATION

Every application for registration should be accompanied by a non-refundable application fee as specified in these regulations. An application, which is not complete in all respects or does not conform to the requirements, should be rejected by SEBI. However, before rejecting any such application, the applicant is given an opportunity to remove within one month such objections as indicated by SEBI. The regulation further provides that SEBI can extend the time where sufficient reason is being given by the applicant that efforts have been taken to remove such deficiency.

CONDITIONS FOR ELIGIBILITY

The applicant should satisfy the following eligibility criteria:

- (a) the applicant is set up and registered as a company under the Companies Act, 2013;
- (b) the applicant has specified the managing of collective investment scheme as one of its main objects in its Memorandum of Association;
- (c) the applicant has a net worth of not less than rupees five crores. However, at the time of making the application, the applicant shall have a minimum net worth of rupees three crores which has to be increased to rupees five crores within the time period of three years from the date of grant of registration;
- (d) the applicant is a fit and proper person for the grant of such certificate;
- (e) the applicant has adequate infrastructure to operate collective investment scheme in accordance with the provision of these regulations;
- (f) the directors or key personnel of the applicant should consist of persons of honesty and integrity having adequate professional experience in related field and have not been convicted for an offence involving moral turpitude or for any economic offence or for the violation of any securities laws;
- (g) at least fifty per cent of the directors of such Collective Investment Management Company shall consist of independent directors and are not directly or indirectly associated with the persons who have control over the Collective Investment Management Company;
- (h) no person, directly or indirectly connected with the applicant has in the past been refused registration by SEBI under the Act;
- (i) at least one of the directors on the board of the Collective Investment Management Company, who is not subject to retirement, is a representative of the trustee;
- (j) the Collective Investment Management Company is not a trustee of any collective investment scheme.
- (k) in case the applicant is an existing collective investment scheme, it complies with the provisions of Chapter IX of the these regulations.

GRANT OF CERTIFICATE

SEBI shall grant certificate of registration to the applicant on such terms and conditions as in the interest of investors and specified, in case the following is fulfilled:

- An application without deficiencies has been received,
- Applicant has complied with specified requirements,
- Registration fees has been called upon by SEBI and duly paid by the applicant.

TERMS AND CONDITIONS

The certificate granted should be subject to following conditions:

- (a) any director of the CIMC should not be a director in any other CIMC unless such person is an independent director and approval of the Board of CIMC of which such person is an independent director, has been obtained;
- (b) the CIMC should forthwith inform SEBI of any material change in the information or particulars previously furnished, which have a bearing on the certificate granted by it;
- (c) appointment of a director of a CIMC should be made with the prior approval of the trustee;
- (d) the CIMC should comply with provisions of the Act and these regulations;

- (e) no change in the controlling interest of the CIMC shall be made without obtaining prior approval of SEBI, the trustee and the unit holders holding atleast one-half of the nominal value of the unit capital of the scheme.
- (f) CIMC should take adequate steps to redress the grievances of the investors within one month from the date of receipt of the complaint from the aggrieved investor.

PROCEDURE WHERE REGISTRATION IS NOT GRANTED

SEBI may reject the application, if it does not satisfy the conditions specified in regulation. It gives a reasonable opportunity of being heard to the applicant. The decision should be communicated to the applicant by SEBI within 30 days of such decision, stating therein the grounds on which the application has been rejected.

RESTRICTIONS ON BUSINESS ACTIVITIES

The Collective Investment Management Company should not:

- (i) undertake any activity other than that of managing the scheme;
- (ii) act as a trustee of any scheme;
- (iii) launch any scheme for the purpose of investing in securities;
- (iv) invest in any schemes floated by it.

However, it has been provided that a CIMC may invest in its own scheme, if it makes a disclosure of its intention to invest in the offer document of the scheme, and does not charge any fees on its investment in that scheme.

OBLIGATIONS OF COLLECTIVE INVESTMENT MANAGEMENT COMPANY

Every Collective Investment Management Company should:

- (i) be responsible for managing the funds or properties of the scheme on behalf of the unit holders and take all reasonable steps and exercise due diligence to ensure that the scheme is managed in accordance with the provisions of these regulations, the offer document and the trust deed;
- (ii) exercise due diligence and care in managing assets and funds of the scheme and also responsible for the acts of commissions and omissions by its employees or the persons whose services have been availed by it;
- (iii) remain liable to the unit holders for its acts of commission or omissions, notwithstanding anything contrary contained in any contract or agreement and be incompetent to enter into any transaction with or through its associates, or their relatives relating to the scheme. However, in case the CIMC enters into any transactions relating to the scheme with any of its associates, a report to that effect should immediately be sent to the trustee and to SEBI;
- (iv) appoint registrar and share transfer agents and should also abide by their respective Code of Conducts as specified in the Third Schedule;
- (v) give receipts for all monies received and report of the receipts and payments to SEBI, on monthly basis;
- (vi) hold a meeting of Board of Directors to consider the affairs of scheme, at least twice in every three months and also ensures that its officers or employees do not make improper use of their position or information to gain, directly or indirectly, an advantage for themselves or for any other person or to cause detriment to the scheme;
- (vii) obtain adequate insurance against the properties of the schemes and comply with such guidelines, directives, circulars and instructions as may be issued by SEBI from time to time on the subject of Collective Investment Scheme i.e. as the end of March, June, September and December.

SUBMISSION OF INFORMATION AND DOCUMENTS

The Collective Investment Management Company should prepare quarterly reports of its activities and the status of compliance of SEBI regulations and submit the same to the trustees within one month of the expiry of each quarter. The Collective Investment Management Company should file with the trustees and SEBI, particulars of all its directors along with their interest in other companies within fifteen days of their appointment. It should furnish a copy of the Balance Sheet, Profit and Loss Account; a copy of the summary of the yearly appraisal report and such other information as may be required, to the unit holders, to SEBI and the trustees within two months from the closure of financial year.

TRUSTEES AND THEIR OBLIGATIONS

A scheme should be constituted in the form of a trust and the instrument of trust should be framed in the form of a deed duly registered under the provisions of the Indian Registration Act, 1908 executed by the CIMC in favour of the trustees named in such an instrument. It can appoint a trustee under the deed to hold the assets of the scheme for the benefit of unit holders.

CONTENTS OF TRUST DEED

The trust deed should contain such clauses as are specified and other clauses as are necessary for safeguarding the interests of the unit holders. No trust deed should contain a clause which has the effect of limiting or extinguishing the obligations and liabilities of the Collective Investment Management Company in relation to any scheme or the unit holders; or indemnifying the trustee or the Collective Investment Management Company for loss or damage caused to the unit holders by their acts of negligence or acts of commissions or omissions.

ELIGIBILITY FOR APPOINTMENT AS TRUSTEE

The persons registered with SEBI as Debenture Trustee under SEBI (Debenture Trustee) Regulations, 1993 are only eligible to be appointed as trustees of collective investment schemes. However, no person is eligible to be appointed as trustee, if he is directly or indirectly associated with the persons who have control over the CIMC. The CIMC shall furnish to SEBI particulars in respect of trustees appointed in the prescribed form.

No person should be appointed as trustee of a scheme, if he has been found guilty of an offence under the securities laws or SEBI or any authority to which SEBI has delegated its power has passed against such person, an order under the Act for violation of any provision of the Act or of regulations made hereunder.

The trustee and the Collective Investment Management Company should enter into an agreement for managing the schemes' property. The agreement for managing the scheme property should contain clauses as specified and such other clauses as are necessary for the purpose of fulfilling the objectives of the scheme.

RIGHTS AND OBLIGATIONS OF THE TRUSTEE

The trustee have a right to obtain from the CIMC such information as is considered necessary by the trustee and to inspect the books of accounts and other records relating to the scheme. The trustee should ensure that the CIMC has;

- (i) the necessary office infrastructure;
- (ii) appointed all key personnel including managers for the schemes and submitted their bio-data which shall contain the educational qualifications and past experience in the areas relevant for fulfilling the objectives of the schemes;
- (iii) appointed auditors from the list of auditors approved by SEBI to audit the accounts of the scheme;
- (iv) appointed a compliance officer to comply with the provisions of the Act and these regulations and to redress investor grievances;

- (v) appointed registrars to an issue and share transfer agent.
- (vi) prepared a compliance manual and designed internal control mechanisms including internal audit systems;
- (vii) taken adequate insurance for the assets of the scheme;
- (viii) not given any undue or unfair advantage to any associates of the company or dealt with any of the associates in any manner detrimental to the interest of the unit holders;
- (ix) operated the scheme in accordance with the provisions of the trust deed, these regulations and the offer document of the scheme(s);
- (x) undertaken the activity of managing schemes only;
- (xi) taken adequate steps to ensure that the interest of investors of one scheme are not compromised with the object of promoting the interest of investors of any other scheme;
- (xii) minimum networth on a continuous basis and shall inform SEBI immediately of any shortfall;
- (xiii) been diligent in empanelling the marketing agents and in monitoring their activities.

The trustee should forthwith take such remedial steps as are necessary and immediately inform SEBI of the action taken where the trustee believes that the conduct of business of the scheme is not in accordance with the regulations. The trustee should be accountable for, and act as the custodian of the funds and property of the respective schemes and should hold the same in trust for the benefit of the unit holders in accordance with these regulations and the provisions of trust deed. The trustee should be responsible for the calculation of any income due to be paid to the scheme and also for any income received in the scheme to the unit holders. The trustee is required to convene a meeting of the unit holders on requisition of SEBI or unit holders holding at least one-tenth of nominal value of the unit capital of any scheme or when any change in the fundamental attributes of any scheme which affects the interest of the unit holders is proposed to be carried out. However, no such change should be carried out unless the consent of unit holders holding at least three-fourths of nominal value of the unit capital of the scheme is obtained.

The trustee should review on a quarterly basis i.e. by the end of March, June, September, and December every year :

- all activities carried out by the CIMC;
- periodically all service contracts relating to registrars to an issue and share transfer agents and satisfy itself that such contracts are fair and reasonable in the interest of the unit holders;
- investor complaints received and the redressal of the same.

The trustee should ensure that net worth of CIMC is not deployed in a manner which is detrimental to interest of unit holders and also that the property of each scheme is clearly identifiable as scheme property and held separately from property of the CIMC. Clearances or no objection certificate should be obtained, in respect of transactions relating to property of the scheme from such authority as is competent to grant such clearance or no objection certificate. The trustee should abide by the Code of Conduct as specified in the Third Schedule. The trustee is required to furnish to SEBI on a quarterly basis every year, a report on the activities of the scheme and a certificate stating that the trustee has satisfied himself that affairs of the Collective Investment Management Company and of the various schemes are conducted in accordance with these regulations and investment objective of each scheme.

The trustee should cause:

- (a) the profit and loss accounts and balance sheet of the schemes to be audited at the end of each financial year by an auditor empanelled with SEBI.
- (b) each scheme to be appraised at the end of each financial year by an appraising agency.
- (c) scheme to be rated by a credit rating agency.

A meeting of the trustees to discuss the affairs of the scheme should be held at least twice in every three months.

The trustee should report to SEBI any breach of these regulations that has, or is likely to have, made materially adverse effect on the interests of unit holders, as soon as they become aware of the breach. The trustee should ensure that the fees and expenses of the scheme are within the limits as specified and the accounts of the schemes are drawn up in accordance with the accounting norms as specified and should comply with accounts of the scheme and the format of the balance sheet and the profit and loss account as specified in these regulation.

TERMINATION OF TRUSTEESHIP

The trusteeship of a trustee should come to an end –

- (a) If the trustee ceases to be trustee under SEBI (Debentures Trustees) Regulations, 1993; or
- (b) if the trustee is in the course of being wound up; or
- (c) if unit holders holding at least three-fourths of the nominal value of the unit capital of the scheme pass a resolution for removing the trustee and SEBI approves such resolution; or
- (d) if in the interest of the unit holders, SEBI, for reasons to be recorded in writing decides to remove the trustee for any violation of the Act or these regulations committed by them or the trustee should be afforded reasonable opportunity of being heard before action is taken under this clause;
- (e) if the trustee serves on the Collective Investment Management Company, a notice of not less than three months expressing intention of not to continue as trustee.

In such cases, another trustee should be appointed by the CIMC on the termination of the trusteeship. The appointment of the new trustee should be completed within three months from the date of termination of the previous trusteeship. If CIMC is unable to appoint trustee in requisite time period of three months, then SEBI can appoint any person as a trustee from its empanelled list. The new trustee appointed should stand substituted as trustee in all the documents, to which the trustee so removed was a party. A trust deed in the prescribed form as specified in these regulation shall be executed by the CIMC in favour of the trustee so appointed and from the date of such appointment trustees shall be subject to all the rights and duties as specified in these regulations. The trustees so removed shall from such date be discharged from complying with the obligations under the trust deed but shall remain liable for any action taken by them before such removal. The person appointed by SEBI should apply to the Court for an order directing the CIMC to wind up the scheme.

TERMINATION OF THE AGREEMENT WITH THE COLLECTIVE INVESTMENT MANAGEMENT COMPANY

The agreement entered into by the trustee with the Collective Investment Management Company may be terminated –

- (a) if the CIMC is in the course of being wound up as per the provisions of the Companies Act, 2013 or;
- (b) if unit holders holding at least three-fourth of the nominal value of the unit capital of the scheme pass a resolution for terminating the agreement with the CIMC and the prior approval of SEBI has been obtained, or
- (c) if in the interest of the unit holders, SEBI or the trustee after obtaining prior approval of SEBI, and after giving an opportunity of being heard to the Collective Investment Management Company, decide to terminate the agreement with the CIMC.

Another CIMC registered with SEBI, should be appointed upon the termination of agreement by the trustee within three months from the date of such termination. The CIMC so removed continues to act as such at the discretion of trustee or the trustee itself may act as CIMC till such time as new CIMC is appointed. The CIMC appointed should stand substituted as a party in all the documents to which the CIMC so removed was a party. The CIMC so removed should continue to be liable for all acts of omission and commissions notwithstanding such termination. If, none of the CIMC, registered under the regulations, consent to be appointed as CIMC within a further period of three months, then the trustee may wind up the scheme. An agreement for managing scheme property should be

executed in favour of the new CIMC subject to all the rights and duties as specified in the regulations.

PROCEDURE FOR LAUNCHING OF SCHEMES

No scheme should be launched by the CIMC unless such scheme is approved by the Trustee and rated by a registered credit rating agency and appraised by an appraising agency.

DISCLOSURES IN THE OFFER DOCUMENT

The CIMC shall before launching any scheme file a copy of the offer document of the scheme with SEBI and pay filing fees as specified. The offer document should contain such information as specified. The offer document should also contain true and fair view of the scheme and adequate disclosures to enable the investors to make informed decision. SEBI may in the interest of investors require the CIMC to carry out such modifications in the offer document as it deems fit. In case no modifications are suggested by SEBI in the offer document within 21 days from the date of filing, the Collective Investment Management Company may issue the offer document to public.

ALLOTMENT OF UNITS AND REFUNDS OF MONEY

The Collective Investment Management Company should specify in the offer document the minimum and the maximum subscription amount it seeks to raise under the scheme; and in case of oversubscription, the process of allotment of the amount oversubscribed. The CIMC should refund the application money to the applicants, if the scheme fails to receive the minimum subscription amount. Any amount refundable should be refunded within a period of six weeks from the date of closure of subscription list, by Registered A.D. and by cheque or demand draft. In the event of failure to refund the amounts within the period specified, the CIMC has to pay interest to the applicants at a rate of fifteen percent per annum on the expiry of six weeks from the date of closure of the subscription list. A scheme shall not be open for more than 90 days.

UNIT CERTIFICATES

The Collective Investment Management Company should issue to the applicant whose application has been accepted, unit certificates as soon as possible but not later than six weeks from the date of closure of the subscription list. However, if the units are issued through a depository, a receipt in lieu of unit certificate will be issued as per provisions of SEBI (Depositories and Participants) Regulations, 1996 and bye-laws of the depository.

TRANSFER OF UNITS

A unit certificate issued under the scheme should be freely transferable. The CIMC on production of instrument of transfer together with relevant unit certificates, register the transfer and return the unit certificate to the transferee within thirty days from the date of such production. However, if the units are held in a depository such units shall be transferable in accordance with the provisions of the SEBI (Depositories and Participants) Regulations, 1996 and bye-laws of the depository.

The subscription amount received should be kept in a separate bank account in the name of the scheme and utilised for –

- (1)(a) adjustment against allotment of units only after the trustee has received a statement from the registrars to the issue and share transfer agent regarding minimum subscription amount, as stated in the offer document, having been received from the public, or
- (b) for refund of money in case minimum subscription amount, as stated in the offer document, has not been received or in case of over-subscription.
- (2) The minimum subscription amount as specified in the offer document couldn't be less than the minimum amount, as specified by the appraising agency, needed for completion of the project for which the scheme is being launched.

- (3) The moneys credited to the account of the scheme should be utilised for the purposes of the scheme and as specified in the offer document.
- (4) Any unutilised amount lying in the account of the scheme should be invested in the manner as disclosed in the offer document.

INVESTMENTS AND SEGREGATION OF FUNDS

The Collective Investment Management Company should:

- (a) not invest the funds of the scheme for purposes other than the objective of the scheme as disclosed in the offer document.
- (b) segregate the assets of different schemes.
- (c) not invest corpus of a scheme in other schemes.
- (d) not transfer funds from one scheme to another scheme.

However, it has been provided that inter scheme transfer of scheme property may be permitted at the time of termination of the scheme with prior approval of the trustee and SEBI.

LISTING OF SCHEMES

The units of every scheme shall be listed immediately after the date of allotment of units and not later than six weeks from the date of closure of the scheme on each of the stock exchanges as mentioned in the offer document.

WINDING UP OF SCHEME

A scheme should be wound up on the expiry of duration specified in the scheme or on the accomplishment of the objective of the scheme as specified in the offer document. A scheme may be wound up :

- (a) on the happening of any event which, in the opinion of the trustee, requires the scheme to be wound up and the prior approval of SEBI is obtained; or
- (b) if unit holders of a scheme holding at least three-fourth of the nominal value of the unit capital of the scheme, pass a resolution that the scheme be wound up and the approval of SEBI is obtained thereto; or
- (c) if in the opinion of SEBI, the continuance of the scheme is prejudicial to the interests of the unit-holders; or
- (d) if in the opinion of the CIMC, the purpose of the scheme cannot be accomplished and it obtains the approval of the trustees and that of the unit holders of the scheme holding at least three-fourth of the nominal value of the unit capital of the scheme with a resolution that the scheme be wound up and the approval of SEBI is obtained thereto.

Where a Scheme is to be wound up, the trustee shall give notice disclosing the circumstances leading the winding up of the Scheme in a daily newspaper having nationwide circulating and in the newspaper published in the language of the region where the CIMC is registered.

The trustee should dispose of the assets of the scheme concerned in the best interest of the unit holders of that scheme. The proceeds of sale realised, should be first utilised towards the discharge of such liabilities as are due and payable under the scheme and after making appropriate provision for meeting the expenses connected with such winding up, the balance shall be paid to the unit holders in proportion to their unit holding. After the completion of the winding up, the trustee should forward to SEBI and the unit holders –

- (a) a report on the steps taken for realisation of assets of the scheme, expenses for winding up and net assets available for distribution to the unit holders, and

- (b) a certificate from the auditors of the scheme to the effect that all the assets of the scheme are realised and the details of the distribution of the proceeds.

The unclaimed money, if any at the time of winding up, should be kept separately in a bank account by the trustee for a period of three years for the purpose of meeting investors' claims and thereafter, should be transferred to investor protection fund, as may be specified by SEBI. On and from the date of the publication of notice, the trustee or the CIMC as the case may be, shall cease to carry on any business activities in respect of the Scheme so wound up.

Requirements with respect to the listing of units or any other instrument of a Collective Investment Scheme on a recognised stock exchange.

A Collective Investment Management Company (CIMC) which is desirous of getting its any collective investment scheme listed on a recognised stock exchange, shall apply for the purpose to the stock exchange and forward along with its application the following documents and particulars :

- (a) Certificate of incorporation, MOA & AOA of the company and the copy of the trust deed of the scheme.
- (b) Copies of all prospectuses or statements in lieu of prospectuses
- (c) Copies of offers for sale and circulars or advertisements offering any unit or other instrument for subscription or sale during the last five years, or in the case of a new company, such shorter period during which the company has been in existence.
- (d) Copies of balance sheets and audited accounts for the last five years, or in the case of a new company, for such completed financial year for which accounts have been made up.
- (e) A statement showing :-
 - (i) returns and cash bonuses, if any, paid during the last ten years (or such shorter period as the company has been in existence whether as a private or public company);
 - (ii) returns or interest in arrears, if any
- (f) Certified copies of agreements or other documents relating to arrangements pertaining to each scheme of the company with or between, –
 - (i) vendors and/or promoters;
 - (ii) underwriters and sub-underwriters;
 - (iii) brokers and sub-brokers
- (g) Certified copies of agreements pertaining to each scheme of a company with—
 - (i) selling agents and other service providers;
 - (ii) managing directors and technical directors;
 - (iii) general manager, sales manager, manager or secretary
- (h) Certified copies of every letter, report, balance sheet, valuation contract, court order or other document, part of which is reproduced or referred to in any prospectus, offer for sale, circular or advertisement offering units or any other instruments of the scheme for subscription or sale, during the last five years.
- (i) A statement containing particulars of the dates of, and parties to all material contracts, agreements (including agreements for technical advice and collaboration), concessions and similar other documents (except those entered into in the ordinary course of business carried on or intended to be carried on by the company) together with a brief description of the terms, subject-matter and general nature of the documents pertaining to such scheme.

- (j) A brief history of the Company since its incorporation giving details of its activities including any re-organization, reconstruction or amalgamation, changes in its capital structure (authorised, issued and subscribed) and debenture borrowings, if any, and the performance of other collective investment schemes of the company.
 - (k) Particulars of units of the scheme and/or shares, debentures of the company issued :-
 - i. for consideration other than cash, whether in whole or part,
 - ii. at a premium or discount, or
 - iii. in pursuance of an option.
 - (l) A statement containing particulars of any commission, brokerage, discount or other special terms granted to any person pertaining to such scheme.
 - (m) Certified copies of :-
 - (i) certificate of registration granted by SEBI;
 - (ii) acknowledgement card or the receipt of filing offer document with SEBI;
 - (iii) agreements, if any, with any public financial institution as specified in section 2(72) of the Companies Act, 2013.
 - (n) A list of the highest ten holders of units of each scheme of the company as on the date of application along with particulars as to the number of units held by and the address of each such holder.
 - (o) Particulars of units of the scheme for which permission to deal is applied for. However, a recognised stock exchange may either generally by its bye-laws or in any particular case call for such further particulars or documents as it deems proper.
- (2) Apart from complying with such other terms and conditions as may be laid down by a recognised stock exchange, an applicant shall satisfy the stock exchange that :
- (a) Its AOA provide for the following among others that –
 - (i) The company shall use a common form of transfer of units of a particular scheme;
 - (ii) The fully paid units issued under the scheme will be free from all lien, while in the case of partly paid units the company's lien, if any, will be restricted to moneys called or payable at a fixed time in respect of such units;
 - (iii) Any amount paid-up in advance of calls on any units may carry interest but shall not entitle the holder of the unit to participate in respect thereof, in a return subsequently declared;
 - (iv) There will be no forfeiture of unclaimed returns before the claim becomes barred by law;
 - (v) Option or right to call of units shall not be given to any person except with the sanction of the company in general meeting.
- However, a recognised stock exchange may provisionally admit to dealings the units of a scheme which undertakes to amend its AOA at its next general meeting so as to fulfil the foregoing requirements and agrees to act in the meantime strictly in accordance with the provisions of this clause.
- (b) At least twenty-five per cent of the units or any other instrument of a scheme issued by the company was offered to the public for subscription through advertisement in newspapers for a period not less than two days and not more than ninety days, and that applications received in pursuance of such offer were allotted fairly and unconditionally.

However, a recognised stock exchange may relax this requirement, with the previous approval of the SEBI in respect of a Government company within the meaning of section 2(45) of the Companies Act, 2013 and subject to such instructions as SEBI may issue in this behalf from time to time.

(3) A company applying for listing of a scheme shall, as a condition precedent, undertake, inter alia, that —

- (a) (i) letters of allotment of units or any other instrument will be issued simultaneously and that, in the event of its being impossible to issue letters of regret at the same time, a notice to that effect will be inserted in the press so that it will appear on the morning after the letters of allotment have been posted;
- (ii) letters of right will be issued simultaneously;
- (iii) letters of allotment, acceptance or rights will be serially numbered, printed on good quality paper and, examined and signed by a responsible officer of the company and that whenever possible, they will contain the distinctive numbers of the units or any other instrument to which they relate;
- (iv) letters of allotment and renounceable letters of right will contain a proviso for splitting and that, when so required by the exchange, the form of renunciation will be printed on the back of or attached to the letters of allotment and letters of right;
- (v) letters of allotment and letters of right will state how the next payment of interest or return on the units or any other instrument will be calculated;
- (b) to issue, when so required, receipts for all units and any other instrument deposited with it whether for registration, sub-division, exchange or for other purposes; and not to charge any fees for registration of transfers, for sub-division and consolidation of units and any other instrument and for sub-division of letters of allotment, renounceable letters of right, and split, consolidation, renewal and transfer receipts into denominations of the market unit of trading;
- (c) to issue, when so required, consolidation and renewal units or any other instrument in denominations of the market unit of trading, to split units or any other instrument, letters of allotment, letters of right, and transfer, renewal, consolidation and split receipts into smaller units, to split call notices, issue duplicates thereof and not require any discharge on call receipts and to accept the discharge of members of stock exchange on split, consolidation and renewal receipts as good and sufficient without insisting on the discharge of the registered holders;
- (d) when documents are lodged for sub-division or consolidation or renewal through the clearing house of the exchange :
 - (i) to accept the discharge of an official of the stock exchange clearing house on the company's split receipts and consolidation receipts and renewal receipts as good and sufficient discharge without insisting on the discharge of the registered holders; and
 - (ii) to verify when the company is unable to issue units or any other instruments or split receipt or consolidation receipts or renewal receipts immediately on lodgement whether the discharge of the registered holders, on the documents lodged for sub-division or consolidation or renewal and their signatures on the relative transfers are in order;
- (e) on production of the necessary documents by unit holders or by members of the exchange, to make on transfers an endorsement to the effect that the power of attorney or probate or letters of administration or death certificate or similar other document has been duly exhibited to and registered by the company;
- (f) to issue certificates in respect of units or any other instrument lodged for transfer within a period of one month of the date of lodgement of transfer and to issue balance units or any other instrument within the same period where the transfer is accompanied by a larger unit or any other instrument certificate;
- (g) to advise the stock exchange of the date of the board meeting at which the declaration or recommendation

of a return or the issue or right or bonus units or any other instrument will be considered;

- (h) to recommend or declare all returns and/or cash bonuses at least five days before the commencement of the closure of its transfer books or the record date fixed for the purpose and to advise the stock exchange in writing of all returns and/or cash bonuses recommended or declared immediately after a meeting of the board of the company has been held to finalise the same;
- (i) To notify the stock exchange of any change –
 - (a) in the company's directorate by death, resignation, removal or otherwise,
 - (b) of managing director,
 - (c) of auditors appointed to audit the books and account of the company;
- (j) To forward to the stock exchange copies of statutory and annual reports and audited accounts of such scheme as soon as issued, including directors' report;
- (k) To forward to the stock exchange as soon as they are issued copies of all other notices and circulars sent to the unit/other instrument holders regarding any important development or resolutions passed by the company affecting the performance of the scheme and to file with the stock exchange certified copies of resolutions of the company as soon as such resolutions become effective;
- (l) To notify the stock exchange prior to intimating the unit/any other instrument holders, of any new issue of units/other instruments whether by way of right, privilege, bonus or otherwise and the manner in which it is proposed to offer or allot the same;
- (m) To notify the stock exchange in the event of re-issue of any forfeited units/other instruments or the issue of units/other instruments held in reserve for future issue;
- (n) To notify the stock exchange of any other alteration of unit capital including calls;
- (o) to close the transfer books only for the purpose of declaration of returns or issue of right or bonus units/ any other instruments in the scheme or for such other purposes as the stock exchange may agree and to give notice to the stock exchange as many days in advance as the exchange may from time to time reasonably prescribe.
- (p) To forward to the stock exchange an annual return immediately after the preparation of annual accounts of at least ten principal holders of each class of units/any other instruments of the company along with particulars as to the number of units/any other instrument held by, and address of, each such holder;
- (q) To grant to unit/any other instrument holders of the scheme the right of renunciation in all cases of issue of rights, privileges and benefits and to allow them reasonable time, not being less than 4 weeks, within which to record, exercise, or renounce such rights, privileges and benefits, and to issue, where necessary, coupons or the company or body corporate concerned may prefer an appeal to the SAT constituted under section 15K of the SEBI Act, 1992 (15 of 1992), and the procedure laid down under SC (Regulation) (Appeal to Securities Appellate Tribunal) Rules, 2000 shall apply to such appeal. The SAT may, after giving the stock exchange an opportunity of being heard, vary or set aside the decision of the stock exchange and thereupon the orders of the SAT shall be carried out by the stock exchange.

(4) A recognised stock exchange may, either at its own discretion or shall in accordance with the orders of the Securities Appellate Tribunal specified above, restore or readmit to dealings any units/other instruments suspended or withdrawn from the list.

(5) All the requirements with respect to listing prescribed by these rules, shall, so far as they may be, also apply to a body corporate constituted by an Act of Parliament or any State Legislature.

However, a recognised stock exchange may relax the requirement of offer to the public for subscription of at least twenty-five per cent of the units or any other instrument of a collective investment scheme issued in respect of a body corporate referred to in this sub-rule with the previous approval of SEBI and also subject to such instructions as SEBI may issue in this behalf from time to time.

(6) SEBI may, at its own discretion or on the recommendation of a recognised stock exchange, waive or relax the strict enforcement of any or all of the requirements with respect of listing prescribed by these rules.

PENAL PROVISIONS

If, a registered collective investment management company violates certain provisions of the regulations, then action in terms of suspension/ cancellation of certificate may be initiated against the entity. Further, SEBI may, in the interests of the securities market and the investors, initiate criminal prosecution under Section 24 of the SEBI Act, apart from passing of directions such as

- (a) requiring the person concerned not to collect any money from investor or to launch any scheme;
- (b) prohibiting the person concerned from disposing of any of the properties of the scheme acquired in violation of the Regulations;
- (c) requiring the person concerned to dispose off the assets of the scheme in a manner as may be specified in the directions;
- (d) requiring the person concerned to refund any money or the assets to the concerned investors along with the requisite interest or otherwise, collected under the scheme;
- (e) prohibiting the person concerned from operating in the capital market or from accessing the capital market for a specified period.

LESSON ROUND UP

- The CIS is any scheme or arrangement made or offered by any person under which (a) the contributions, or payments made by the investors, by whatever name called, are pooled and utilised solely for the purposes of the scheme or arrangement; (b) the contributions or payments are made to such scheme or arrangement by the investors with a view to receive profits, income, produce or property, whether movable or immovable from such scheme or arrangement; (c) the property, contribution or investment forming part of scheme or arrangement, whether identifiable or not, is managed on behalf of the investors; and (d) the investors do not have day to day control over the management and operation of the scheme or arrangement.
- A scheme should be constituted in the form of a trust and the instrument of trust should be in the form of a deed duly registered under the provisions of the Indian Registration Act, 1908 executed by the Collective Investment Management Company in favour of the trustees named in such an instrument.
- Collective Investment Management Company is regulated by SEBI (Collective Investment Schemes) Regulations, 1999.
- SEBI (Collective Investment Schemes) Regulations, 1999 defines Collective Investment Management Company to mean a company incorporated under the Companies Act, 2013 and registered with SEBI under these regulations, whose object is to organize, operate and manage a collective investment scheme.
- The trustee have a right to obtain from the Collective Investment Management Company such information as is considered necessary by the trustee and to inspect the books of accounts and other records relating to the scheme.

- The units of every scheme shall be listed immediately after the date of allotment of units and not later than six weeks from the date of closure of the scheme on each of the stock exchanges as mentioned in the offer document.
- A scheme should be wound up on the expiry of duration specified in the scheme or on the accomplishment of the purpose of the scheme.

GLOSSARY

Fundamental Attributes	It means the investment objective and terms of a scheme.
Pooling	Pooling is the basic concept behind collective investments. The money of thousands of individual investors, who share a common investment objective, is pooled together to form a CIS portfolio.
Portfolio Manager	The portfolio or investment manager acts as the channel through which the investors invest their money. The portfolio manager is therefore responsible for investing the pool of investors' money. He or she will decide which securities to hold, when to buy or when to sell.
Trustee	The persons registered with SEBI as Debenture Trustee under SEBI (Debenture Trustee) Regulations, 1993 are only eligible to be appointed as trustees of collective investment scheme.

SELF TEST QUESTIONS

1. What are the obligations of Collective Investment Management Company?
2. Discuss the various restrictions on business activities of Collective Investment Management Company?
3. Enumerate the rights and obligations of trustees of collective investment schemes?
4. Discuss the circumstances under which a collective investment scheme could be wound up?

Lesson 10

Resource Mobilisation In International Capital Market

LESSON OUTLINE

- Introduction
- Regulatory Framework in India
- Depository Receipts
- ADR and GDR
- Depository Receipts Scheme, 2014
- Sponsored ADR/GDR Issue
- Two-Way Fungibility Scheme
- Provisions of Companies Act, 2013 relating to issue of GDR
- Companies (Issue of Global Depository Receipts) Rules, 2014
- Procedure for Issuance of GDR/FCCBs
- Appointment of Intermediaries
- Principal Documentation
- Pre and Post Launch – Additional Key Actions
- Foreign Currency Exchangeable Bonds
- Difference Between FCCB and FCEB
- Issue of Foreign Currency Exchangeable Bonds (FCEB) Scheme, 2008
- Foreign Currency Convertible Bonds
- FCCB and Ordinary Shares (Through Depository Receipt Mechanism) Scheme, 1993
- External Commercial Borrowing
- LESSON ROUND UP
- GLOSSARY
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

With the advent of globalization in securities markets, the walls of domestic capital markets got eroded, facilitating the companies to tap foreign sources of capital that demanded lower rates of return. India being an emerging market has been following the trend and the reforms has started since 1991. The Government of India has taken various policies initiatives to allow India companies to raised funds from International Market. It includes implementation of FCCB and Ordinary Share (through Depository Receipt Mechanism) Scheme 1993, Foreign Currency Exchangeable Bonds Scheme 2008, the Consolidated FDI Policy and Depository Receipts Scheme, 2014. The Ministry of Corporate Affairs has notified Companies (Issue of Global Depository Receipts) Rules, 2014 for Issue of GDR. These policy initiatives have lead to the introduction of International Instruments like American Depository Receipts (ADR), Global Depository Receipts (GDR), Foreign Currency Convertible Bonds (FCCBs) and Foreign currency Exchangeable Bonds (FCEBs) etc.

A student should know about the choice of instruments through which a company can mobilise funds from foreign market to have optimum capital structure.

Keeping this in view, this lesson will explain the basics of different modes of Euro issue like ADR, FDR, FCCB, FCEB, their advantages, the regulatory framework governing such type of fund raising, documentation required in this procedure, key intermediaries involved, approval required for such fund raising External Commercial Borrowings etc.

INTRODUCTION

Increased globalization and investor appetite for diversification, offer a unique opportunity to companies looking to tap a new investor base, awareness or raise capital. Indian companies are allowed to raise equity capital in the international market through the issue of GDR/ADR/FCCB/FCEB.

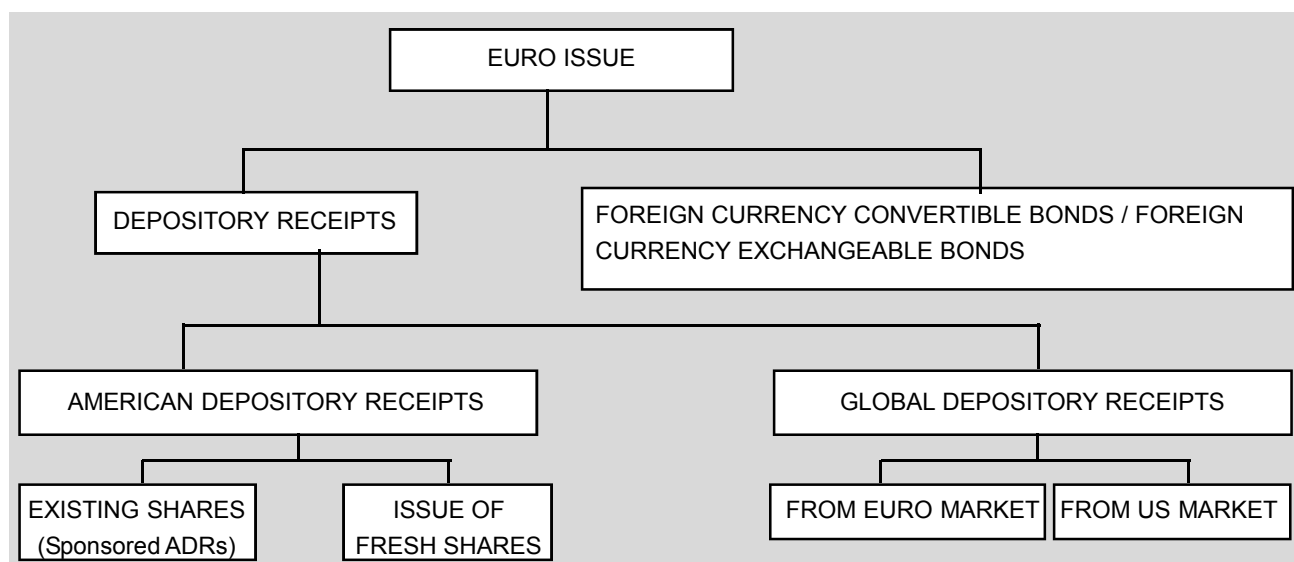
REGULATORY FRAMEWORK IN INDIA

Issue of ADR/GDR/FCCBs/FCEBs are regulated by the following regulations in India:

- The Foreign Currency Convertible Bonds and Ordinary Shares (Through Depository Receipt Mechanism) Scheme, 1993.
- Foreign Currency Exchangeable Bonds Scheme, 2008
- Depository Receipts Scheme, 2014
- Notifications/Circulars issued by Ministry of Finance (MoF), GOI.
- Consolidated FDI Policy.
- RBI Regulations/Circulars.
- Companies Act and Rules thereunder.
- Listing Regulations.

EURO ISSUE

Euro issue means modes of raising funds by an Indian company outside India in foreign currency. There are different modes of Euro issue which is as follows:



DEPOSITORY RECEIPTS

Depository Receipt (DR) is a negotiable instrument evidencing a fixed number of equity shares of the issuing company being an Indian company, denominated in foreign currency and is being traded in foreign exchanges.

Why do Company Issue Depository Receipts

Company issues DRs as a tool to access Global capital markets. Following are the some reason for issuing DRs by a company –

- To raise capital;
- Diversify Shareholder base into extended geographies;
- Increase visibility & recognition in international market;
- Global Image;
- Set Up Employee Stock Option Plans;
- Facilitate Merger & Acquisition activity by creating a desirable acquisition currency.

Purpose of Investors to Invest in Depository Receipts

- Diversify Portfolio
- Convenience of holding foreign securities in their markets
- Simplification of trading and settlements(DRs trade and settle just like US or EURO securities)
- No restrictions on dealing: DRs are recognized as domestic securities
- Avoid Currency risk.

ADR & GDR

An American Depository Receipt (“ADR”) is a dollar denominated form of equity ownership in the form of depository receipts in a non-US company. It represents the foreign shares of the company held on deposit by a custodian bank in the company’s home country and carries the corporate and economic rights of the foreign shares.

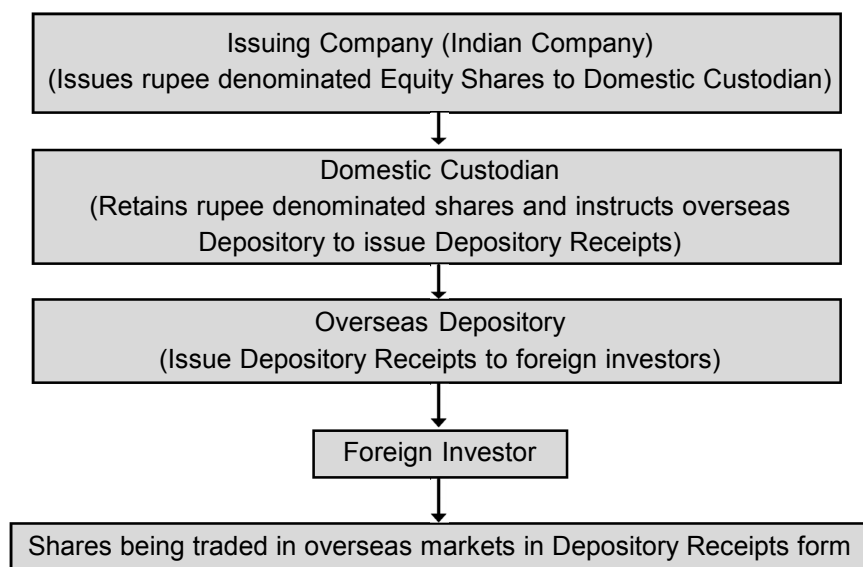
GDRs have access usually to Euro market and US market. The US portion of GDRs to be listed on US exchanges to comply with SEC requirements and the European portion are to be complied with EU directive. Listing of GDR may take place in international stock exchanges such as London Stock Exchange, New York Stock Exchange, American Stock Exchange, NASDAQ, Luxemburg Stock Exchange etc.

Difference between American Depository Receipts (ADR) and Global Depository Receipts (GDR)

ADR are US \$ denominated and traded in US.

GDRs are traded in various places such as New York Stock Exchange, London Stock Exchange, etc.

PROCESS INVOLVED IN ISSUE OF DEPOSITORY RECEIPTS



ISSUE OF ADR/GDR

Depository Receipts (DRs) means a negotiable security issued outside India by a Depository bank, on behalf of an Indian company, which represent the local Rupee denominated equity shares of the company held as deposit by a Custodian bank in India. DRs are traded on Stock Exchanges in the US, Singapore, Luxembourg, London, etc. DRs listed and traded in the US markets are known as American Depository Receipts (ADRs) and those listed and traded elsewhere are known as Global Depository Receipts (GDRs). In the Indian context, DRs are treated as FDI.

- (a) FCCBs/DRs may be issued in accordance with the Scheme for issue of Foreign Currency Convertible Bonds and Ordinary Shares (Through Depository Receipt Mechanism) Scheme, 1993 and DR Scheme 2014 respectively, as per the guidelines issued by the Government of India thereunder from time to time.
- (b) DRs are foreign currency denominated instruments issued by a foreign Depository in a permissible jurisdiction against a pool of permissible securities issued or transferred to that foreign depository and deposited with a domestic custodian.
- (c) In terms of Notification No. FEMA.20/2000-RB dated May 3, 2000 as amended from time to time, a person will be eligible to issue or transfer eligible securities to a foreign depository, for the purpose of converting the securities so purchased into depository receipts in terms of Depository Receipts Scheme, 2014 and guidelines issued by the Government of India thereunder from time to time.
- (d) A person can issue DRs, if it is eligible to issue eligible instruments to person resident outside India under Schedules 1, 2, 2A, 3, 5 and 8 of Notification No. FEMA 20/2000-RB dated May 3, 2000, as amended from time to time.
- (e) The aggregate of eligible securities which may be issued or transferred to foreign depositories, along with eligible securities already held by persons resident outside India, shall not exceed the limit on foreign holding of such eligible securities under the relevant regulations framed under FEMA, 1999.
- (f) The pricing of eligible securities to be issued or transferred to a foreign depository for the purpose of issuing depository receipts should not be at a price less than the price applicable to a corresponding mode of issue or transfer of such securities to domestic investors under the relevant regulations framed under FEMA, 1999.
- (g) The issue of depository receipts as per DR Scheme 2014 shall be reported to the Reserve Bank of India by the domestic custodian as per the reporting guidelines for DR Scheme 2014.

DEPOSITORY RECEIPTS SCHEME, 2014

The Ministry of Finance, on October 21, 2014, notified the Depository Receipts Scheme, 2014, amending and repealing the issue of Foreign Currency Convertible Bonds and Ordinary Shares (Through Depository Receipt Mechanism) Scheme, 1993, to the extent applicable to the issuance of depository receipts. The Scheme was implemented, pursuant to the recommendations of the Sahoo committee to Review the FCCBs and Ordinary Shares (Mechanism) Scheme, 1993, with a view to increase participation by Indian companies in overseas financial markets and to facilitate raising of capital from global investors. The Scheme, governing the issue depository receipts, came into force from December 15, 2014.

Depository Receipts are generally classified as under:

Sponsored

A sponsored issue of depository receipts is based on a stock agreement, between the foreign depository and the issuer of securities for the creation of the depository receipts. The sponsored depository receipts can be further classified as:

Capital Raising: The Indian issuer deposits the freshly issued securities with the domestic custodian. On the basis of such deposit, the foreign depository then creates/issues depository receipts abroad for sale to global investors. This constitutes a capital raising exercise, as the proceeds of the sale of depository receipts eventually go to the Indian issuer.

Non-Capital Raising: In a non-capital raising issue, no fresh underlying securities are issued. Rather, the issuer gets holders of its existing securities to deposit these securities with a domestic custodian, so that depository receipts can be issued abroad by the foreign depository. This is not a capital raising exercise for the Indian issuer, as the proceeds from the sale of the depository receipts go to the holders of underlying securities.

Un-sponsored

Where there is no stock agreement between the foreign depository and the Indian issuer, any person, without any involvement of the issuer, may deposit the securities with a domestic custodian in India. A foreign depository then issues depository receipts abroad on the back of such deposited underlying securities. The proceeds from the sale of such depository receipts go to the holders of the underlying securities. Based on whether a depository receipt is traded in an organised market or in the Over the Counter (“OTC”) market, the depository receipts can be classified as listed or unlisted.

Listed: Listed depository receipts are traded on stock exchanges.

Unlisted: The unlisted depository receipts are those which are inter-traded between parties and where such depository receipts are not listed on any stock exchanges.

DEFINITIONS

Permissible Jurisdiction

‘Permissible Jurisdiction’ as foreign jurisdiction which is a member of the Financial Action Task Force on Money Laundering and the regulator of the securities market in that jurisdiction is a member of the International Organization of Securities Commission. Schedule I of the scheme gives the list of permissible jurisdiction.

Permissible securities

‘Permissible securities’ mean ‘securities’ as defined under section 2(h) of the Securities Contracts (Regulation) Act, 1956 and include similar instruments issued by private companies which:

- (i) may be acquired by a person resident outside India under the Foreign Exchange Management Act, 1999: and
- (ii) is in dematerialised form.

Right to issue voting instruction

‘Right to issue voting instruction’ means the right of a depository receipt holder to direct the foreign depository to vote in a particular manner on its behalf in respect of permissible securities.

ELIGIBILITY FOR ISSUE OF DEPOSITORY RECEIPTS

Clause 3 of the scheme describes the eligibility of issue of depository receipts. The following persons are eligible to issue or transfer permissible transactions to a foreign depository for the issue of depository receipts:

- Any Indian company, listed or unlisted, private or public;
- Any other issuer of permissible securities;
- Any person holding permissible securities

which has not been specifically prohibited from accessing the capital market or dealing in securities. Un-sponsored

depository receipts on the back of the listed permissible securities can be issued only if such depository receipts gave the holder the right to issue voting instruction and are listed on an international exchange.

ISSUE OF DEPOSITORY RECEIPTS

- The aggregate of permissible securities which may be issued or transferred to foreign depositories for issue of depository receipts, along with permissible securities already held by persons resident outside India shall not exceed the limit on foreign holding of such permissible securities under the FEMA, 1999;
- The depository receipts may be converted to underlying permissible securities and vice versa;
- A foreign depository may issue depository receipts by way of a public offering or private placement or in any other manner prevalent in a permissible jurisdiction;
- An issuer may issue permissible securities to a foreign depository for the purpose of issue of depository receipts by any mode permissible for issue of such permissible securities to investors;
- The holders of permissible securities may transfer permissible securities to a foreign depository for the purpose of the issue of depository receipt, with or without the approval of issue of such permissible securities through transactions on a recognized stock exchange, bilateral transactions or by tendering through a public platform;
- The permissible securities shall not be issued to a foreign depository for the purpose of issuing depository receipts at a price less than the price applicable to a corresponding mode of issue of such securities to domestic investors under the applicable laws;

Any approval necessary for issue or transfer of permissible securities to a person resident outside India shall apply to the issue or transfer of such permissible securities to a foreign depository for the purpose of issue of depository receipts. Subject to this the issue of depository receipts shall not require any approval from any government agency, if the issuance is in accordance with the scheme.

RIGHTS AND DUTIES

The following are the rights and duties for the foreign depository:

- The foreign depository shall be entitled to exercise voting rights, if any, associated with the permissible securities whether pursuant to voting instruction from the holder of depository receipts or otherwise;
- The shares of a company underlying the depository receipts shall form part of the public shareholding of the company under Securities Contracts (Regulation) Rules, 1957, if:
 1. the holder of such depository receipts has the right to issue voting instruction; and
 2. such depository receipts are listed on an international exchange;
- In the cases not covered under second point, shares of the company underlying depository receipts shall not be included in the total shareholding and in the public shareholding for the purpose of computing the public shareholding of the company;

A holder of depository receipts issued on the back of equity shares of a company shall have the same obligations as if it is the holder of the underlying equity shares, if it has the right to issue voting instruction.

OBLIGATIONS

Clause 8 of the scheme imposes certain obligations on the domestic custodian which are-

- to ensure that the relevant provisions of the scheme related to the issue and cancellation of depository receipts is complied with;

- to maintain records in respect of, and report to, Indian depositories all transactions in the nature of issue and cancellation of depository receipts for the purpose of monitoring limits under the FEMA, 1999;
- to provide the information and data as may be called upon by SEBI, the RBI, Ministry of Finance, Ministry of Corporate Affairs and any other authority of law; and
- to file with SEBI a copy of the document by whatever name called, which sets the terms of issue of depository receipts issued on the back of securities, as defined under Section 2(h) of SCRA, 1956, in a permissible jurisdiction.

The following are the obligations imposed on the Indian Depositories that-

- they shall co-ordinate among themselves;
- they shall disseminate the outstanding permissible securities against which the depository receipts are outstanding; and
- they shall disseminate the limit up to which permissible securities can be converted to depository receipts.

A person issuing or transferring permissible securities to a foreign depository for the purpose of the issue of depository receipts shall comply with relevant provisions of the Indian law, including the scheme, related to the issue and cancellation of depository receipts.

APPROVAL

Any approval necessary for issue or transfer of permissible securities to a person resident outside India shall apply to the issue or transfer of such permissible securities to a foreign depository for the purpose of issue of depository receipts. No approval is required if the issue of depository receipt is in accordance with the scheme.

PRICING

Price of permissible securities issued to foreign depository for the purpose of issuing depository receipts shall not be less than price if such security issued to domestic investors.

Explanation I:

A company listed or proposed to be listed on a recognised stock exchange shall not issue equity shares on preferential allotment to a foreign depository for the purpose of issue of depository receipts at a price less than the price applicable to preferential allotment of equity shares of the same class to investors under ICDR.

Explanation II:

Whereas a listed company makes a qualified institutional placement of permissible securities to a foreign depository for the purpose of issue of depository receipts, the minimum pricing norms of such placement is applicable under the SEBI (ICDR) Regulations, 2009 shall be complied with.

Example: XYZ Limited, a listed company makes a Qualified Institution Placement of shares and the Floor price comes at Rs 60 per share after complying with pricing norms of ICDR Regulations. Now, if same class of shares is being issued to foreign depository for the purpose of issuing DRs, price cannot be less than Rs. 60 and minimum price regulation of SEBI (ICDR) Regulations, 2009 shall be complied with.

SPONSORED ADR/GDR ISSUE

An Indian company can also sponsor an issue of ADR / GDR. Under this mechanism, the company offers its resident shareholders a choice to submit their shares back to the company so that on the basis of such shares, ADRs / GDRs can be issued abroad. The proceeds of the ADR / GDR issue are remitted back to India and distributed among the resident investors who had offered their Rupee denominated shares for conversion. These proceeds can be kept in Resident Foreign Currency (Domestic) accounts in India by the resident shareholders who have tendered such shares for conversion into ADRs / GDRs.

TWO-WAY FUNGIBILITY SCHEME

A limited two-way Fungibility scheme has been put in place by the Government of India for ADRs / GDRs. Under this Scheme, a stock broker in India, registered with SEBI, can purchase shares of an Indian company from the market for conversion into ADRs/GDRs based on instructions received from overseas investors. Re-issuance of ADRs / GDRs would be permitted to the extent of ADRs / GDRs which have been redeemed into underlying shares and sold in the Indian market.

TERM ONE SHOULD KNOW

One way fungibility – Here investors could cancel their depository receipt and recover the proceeds by selling the underlying shares in the Indian market; DRs once redeemed could not be converted into shares.

Two way fungibility – It means that the shares so released can be reconverted by the company into DRs for purchase by the overseas investors. It implies that the re-issuance of DRs would be permitted to the extent of DRs that have been redeemed and underlying shares are sold in domestic market.

Sponsor – It is a process of disinvestment by the Indian shareholders of their holding in overseas market.

PROVISIONS OF COMPANIES ACT, 2013 RELATING TO ISSUE OF GDR

The New Companies Act, 2013 has laid down provisions for issue of Global Depository receipts under Section 41 and The Companies (Issue of Global Depository Receipts) Rules, 2014.

According to Section 2(44) of Companies Act, 2013, “Global Depository Receipt” means any instrument in the form of a depository receipt, by whatever name called, created by a foreign depository outside India and authorised by a company making an issue of such depository receipts;

Section 41 provides that a company may, after passing a special resolution in its general meeting, issue depository receipts in any foreign country in such manner, and subject to such conditions, as may be prescribed.

Companies (Issue of Global Depository Receipts) Rules, 2014

Eligibility to issue depository receipts

Rule 3 lays down that a company may issue depository receipts provided it is eligible to do so in terms of the Scheme and relevant provisions of the Foreign Exchange Management Rules and Regulations.

Conditions for issue of depository receipts

Rule 4 lays down the following conditions to be fulfilled by a company for issue of depository receipts:

- (1) The Board of Directors of the company intending to issue depository receipts shall pass a resolution authorising the company to do so.
- (2) The company shall take prior approval of its shareholders by a special resolution to be passed at a general meeting. However, a special resolution passed under section 62 of Companies Act, 2013 for issue of shares underlying the depository receipts, shall be deemed to be a special resolution for the purpose of section 41 of Companies Act, 2013 as well.
- (3) The depository receipts shall be issued by an overseas depository bank appointed by the company and the underlying shares shall be kept in the custody of a domestic custodian bank.
- (4) The company shall ensure that all the applicable provisions of the Scheme and the rules or regulations or guidelines issued by the Reserve Bank of India are complied with before and after the issue of depository receipts.
- (5) The company shall appoint a merchant banker or a practising chartered accountant or a practising cost accountant or a practising company secretary to oversee all the compliances relating to issue of depository receipts and the compliance report taken from such merchant banker or practising chartered accountant

or practising cost accountant or practising company secretary, as the case may be, shall be placed at the meeting of the Board of Directors of the company or of the committee of the Board of directors authorised by the Board in this regard to be held immediately after closure of all formalities of the issue of depository receipts.

However, that the committee of the Board of directors referred to above shall have at least one independent director in case the company is required to have independent directors.

Manner and form of depository receipts

Rule 5 deals with the manner and form of issue of depository receipts.

- (1) The depository receipts can be issued by way of public offering or private placement or in any other manner prevalent abroad and may be listed or traded in an overseas listing or trading platform.
- (2) The depository receipts may be issued against issue of new shares or may be sponsored against shares held by shareholders of the company in accordance with such conditions as the Central Government or Reserve Bank of India may prescribe or specify from time to time.
- (3) The underlying shares shall be allotted in the name of the overseas depository bank and against such shares, the depository receipts shall be issued by the overseas depository bank abroad.

Voting rights

Rule 6 provides the provisions for voting rights of depository receipts holder.

- (1) A holder of depository receipts may become a member of the company and shall be entitled to vote as such only on conversion of the depository receipts into underlying shares after following the procedure provided in the Scheme and the provisions of this Act.
- (2) Until the conversion of depository receipts, the overseas depository shall be entitled to vote on behalf of the holders of depository receipts in accordance with the provisions of the agreement entered into between the depository, holders of depository receipts and the company in this regard.

Proceeds of Issue

Rule 7 provides that the proceeds of issues of depository receipts shall either be remitted to a bank account in India or deposited in an Indian bank operating abroad or any foreign bank (which is a Scheduled Bank under the Reserve Bank of India Act, 1934) having operations in India with an agreement that the foreign bank having operations in India shall take responsibility for furnishing all the information which may be required and in the event of a sponsored issue of Depository Receipts, the proceeds of the sale shall be credited to the respective bank account of the shareholders.

Non applicability of certain provisions of the Act

- (1) The provisions of the Act and any rules issued thereunder insofar as they relate to public issue of shares or debentures shall not apply to issue of depository receipts abroad.
- (2) The offer document, by whatever name called and if prepared for the issue of depository receipts, shall not be treated as a prospectus or an offer document within the meaning of this Act and all the provisions as applicable to a prospectus or an offer document shall not apply to a depository receipts offer document.
- (3) Notwithstanding anything contained under section 88 of the Companies Act, 2013, until the redemption of depository receipts, the name of the overseas depository bank shall be entered in the Register of Members of the company.

PROCEDURE FOR ISSUANCE OF GDR/FCCBS

APPROVALS REQUIRED

The issue of GDRs/FCCBs requires the approval of a Board of Directors, shareholders, "In principle and Final" approval of Ministry of Finance, approval of Reserve Bank of India, In-principle consent of Stock Exchange for listing of underlying shares and In-principle consent of Financial institutions.

Approval of Board of Directors

A meeting of Board of Directors is required to be held for approving the proposal to raise money from Euro Capital market. A board resolution is to be passed to approve the raising of finance by issue of GDRs/FCCBs. The resolution should indicate therein specific purposes for which funds are required, quantum of the issue, country in which issue is to be launched, time of the issue etc. A director/Sub- Committee of Board of Directors is also to be authorised for seeking Government approval in connection with Euro issue and signing agreements with depository, organising road shows for fixation of price of GDRs. The Board meeting shall also decide and approve the notice of Extraordinary general meeting of shareholders at which special resolution is to be considered.

Approval of Shareholders

Proposal for making Euro issue, as proposed by Board of Directors require approval of shareholders. A special resolution under Section 62 of the Companies Act, 2013 is required to be passed at a duly convened general meeting of the shareholders of the company.

Approval of Ministry of Finance – “In Principle and Final”

In case of FCCB issue exceeding US \$ 100 million, the company needs to apply to Ministry of Finance for approval.

With respect to ADR/GDR, guidelines issued on the subject dated 19-1-2000 brought ADR/GDR under the automatic route and therefore the requirement of obtaining approval of Ministry of Finance, Department of Economic Affairs has been dispensed with.

Further, private placement of ADR/GDR will also not require prior approval provided the issue is managed by investment banker.

Procedure for Getting Approval

Where the approval is required, the following procedure is required to be followed:

An eligible issuing company shall make an application to the Government of India, Ministry of Finance, Deptt. of Economic Affairs, New Delhi, for obtaining 'In-principle' approval.

The application should set out in detail the following points:

- (a) Proposed project or expansion or diversification programme with details of cost of project and means of financing.
- (b) The proposed security viz. Global Depository Receipts (GDRs) or American Depository Receipts (ADRs) against underlying shares or Foreign Currency Convertible Bonds.
- (c) In the case of Bonds, particulars of redemption period, rate of interest, time of conversion of bonds to equity shares of the company, price at which such conversion will take place.
- (d) In the case of GDRs/ADRs, the price at which the equity shares will be issued.
- (e) Justification for the foreign issue.
- (f) Other details about the company such as management, financial data, capacity and its utilisation, financial results and management ratios, statutory liabilities, default in respect of interest/installments, of loans from Banks/Financial Institutions. Exports and imports and salient features of the prospective corporate plans and diversification proposals with special reference to foreign exchange requirements.

The Government of India will, if satisfied with the company's proposals, issue an approval in principle granting permission to the company to mobilise foreign currency resources for a specified amount.

On completion of finalisation of issue structure in consultation with the Lead Manager to the issue, the company should obtain the final approval from the Government.

However, in some cases Foreign Investment Promotion Board (FIPB) clearance is necessary before final approval is given by the Finance Ministry.

Both 'in principle and final' approvals are valid for 3 months respectively from the date of issue.

Approval of Reserve Bank of India

The issuer company has to obtain approvals from Reserve Bank of India under circumstances specified under the guidelines issued by the concerned authorities from time to time.

RBI vide its press release dated January 20, 2000 granted general permissions to make an international offering of rupee denominated equity shares of the company by way of issue of ADR/GDR.

FCCB covered under the automatic route requires no RBI approval. FCCB issue which exceeds USD 50 million but does not exceed USD 100 million need to apply to RBI.

In-principle consent of Stock Exchanges for listing of underlying shares

The issuing company has to make a request to the domestic stock exchange for in-principle consent for listing of underlying shares which shall be lying in the custody of domestic custodian. These shares, when released by the custodian after cancellation of GDR, are traded on Indian stock exchanges like any other equity shares.

In-principle consent of Financial Institutions

Where term loans have been obtained by the company from the financial institutions, the agreement relating to the loan contains a stipulation that the consent of the financial institution has to be obtained. The company must obtain in-principle consent on the broad terms of the proposed issue.

APPOINTMENT OF INTERMEDIARIES

The following agencies are normally involved in the Euro issue:

(i) Lead Manager (ii) Co-Lead/Co-Manager (iii) Overseas Depository Bank (iv) Domestic Custodian Banks (v) Listing Agent (vi) Legal Advisors (vii) Printers (viii) Auditors (ix) Underwriter

Lead Manager

The company has to choose a competent lead manager to structure the issue and arrange for the marketing. Lead managers usually charge a fee as a percent of the issue. The issues related to public or private placement, nature of investment, coupon rate on bonds and conversion price are to be decided in consultation with the lead manager.

Co-Lead/Co-Manager

In consultation with the lead manager, the company has to appoint co-lead/co-manager to coordinate with the issuing company/lead manager to make the smooth launching of the Euro issue.

Overseas Depository Bank

It is the bank which is authorised by the issuing company to issue Depository Receipts against issue of ordinary shares or Foreign Currency Convertible Bonds of issuing company.

Domestic Custodian Bank

This is a banking company which acts as custodian for the ordinary shares or Foreign Currency Convertible Bonds of an Indian company, which are issued by it. The domestic custodian bank functions is to co-ordination with the depository bank. When the shares are issued by a company the same are registered in the name of depository and physical possession is handed over to the custodian. The beneficial interest in respect of such shares, however, rests with the investors.

Listing Agent

One of the conditions of Euro-issue is that it should be listed at one or more Overseas Stock Exchanges. The appointment of listing agent is necessary to coordinate with issuing company for listing the securities on Overseas Stock Exchanges.

Legal Advisors

The issuing company should appoint legal advisors who will guide the company and the lead manager to prepare offer document, depository agreement, indemnity agreement and subscription agreement.

Printers

The issuing company should appoint printers of international repute for printing Offer Circular.

Auditors

The role of issuer company's auditors is to prepare the auditors report for inclusion in the offer document, provide requisite comfort letters and reconciliation of the issuer company's accounts between Indian GAAP/UK GAAP/US-GAAP and significant differences between Indian GAAP/UK GAAP/US-GAAP.

Underwriters

It is desirable to get the Euro issue underwritten by banks and syndicates. Usually, the underwriters subscribe for a portion of the issue with arrangements for tie-up for the balance with their clients. In addition, they will interact with the influential investors and assist the lead manager to complete the issue successfully.

PRINCIPAL DOCUMENTATION

The following principal documents are involved: (i) Subscription Agreement (ii) Depository Agreement (iii) Custodian Agreement (iv) Agency Agreement (v) Trust Deed

Subscription Agreement

Subscription agreement provides that Lead Managers and other managers agree, severally and not jointly, with the company, subject to the satisfaction of certain conditions, to subscribe for GDRs at the offering price set forth. It may provide that obligations of managers are subject to certain conditions precedent.

Subscription agreement may also provide that for certain period from the date of the issuance of GDR the issuing company will not (a) authorise the issuance of, or otherwise issue or publicly announce any intention to issue; (b) issue offer, accept subscription for, sell, contract to sell or otherwise dispose off, whether within or outside India; or (c) deposit into any depository receipt facility, any securities of the company of the same class as the GDRs or the shares or any securities in the company convertible or exchangeable for securities in the company of the same class as the GDRs or the shares or other instruments representing interests in securities in the company of the same class as the GDRs or the shares.

Subscription agreement also provides, an option to be exercisable within certain period after the date of offer circular, to the lead manager and other managers to purchase upto a certain prescribed number of additional GDRs solely to cover over-allotments, if any.

Depository Agreement

Depository agreement lays down the detailed arrangements entered into by the company with the Depository, the forms and terms of the depository receipts which are represented by the deposited shares. It also sets forth the rights and duties of the depository in respect of the deposited shares and all other securities, cash and other property received subsequently in respect of such deposited shares. Holders of GDRs are not

parties to deposit agreement and thus have no contractual rights against or obligations to the company. The depository is under no duty to enforce any of the provisions of the deposit agreement on behalf of any holder or any other person. Holder means the person or persons registered in the books of the depository maintained for such purpose as holders. They are deemed to have notice of, be bound by and hold their rights subject to all of the provisions of the deposit agreement applicable to them. They may be required to file from time to time with depository or its nominee proof of citizenship, residence, exchange control approval, payment of all applicable taxes or other governmental charges, compliance with all applicable laws and regulations and terms of deposit agreement, or legal or beneficial ownership and nature of such interest and such other information as the depository may deem necessary or proper to enable it to perform its obligations under Deposit Agreement.

The company may agree in the deposit agreement to indemnify the depository, the custodian and certain of their respective affiliates against any loss, liability, tax or expense of any kind which may arise out of or in connection with any offer, issuance, sale, resale, transfer, deposit or withdrawal of GDRs, or any offering document.

Copies of deposit agreement are to be kept at the principal office of Depository and the Depository is required to make available for inspection during its normal business hours, the copies of deposit agreement and any notices, reports or communications received from the company.

Custodian Agreement

Custodian works in co-ordination with the depository and has to observe all obligations imposed on it including those mentioned in the depository agreement. The custodian is responsible solely to the depository. In the case of the depository and the custodian being same legal entity, references to them separately in the depository agreement or otherwise may be made for convenience and the legal entity will be responsible for discharging both functions directly to the holders and the company.

Whenever the depository in its discretion determines that it is in the best interests of the holders to do so, it may, after prior consultation with the company terminate, the appointment of the custodian and in such an event the depository shall promptly appoint a successor custodian, which shall, upon acceptance of such appointment, become the custodian under the depository agreement. The depository shall notify holders of such change promptly. Any successor custodian so appointed shall agree to observe all the obligations imposed on him.

Agency Agreement

In case of FCCBs, the company has to enter into an agency agreement with certain persons known as conversion agents. In terms of this agreement, these agents are required to make the principal and interest payments to the holders of FCCBs from the funds provided by the company. They will also liaise with the company at the time of conversion/redemption option to be exercised by the investor at maturity.

Trust Deed

In respect of FCCBs the company enters into a Covenant (known as Trust Deed) with the Trustee for the holders of FCCBs, guaranteeing payment of principal and interest amount on such FCCBs and to comply with the obligations in respect of such FCCBs.

PRE AND POST LAUNCH – ADDITIONAL KEY ACTIONS

Apart from obtaining necessary approvals, appointment of various agencies and proper documentation, the following additional key actions are necessary for making the Euro-issue a success.

(i) Constitution of a Board Sub-Committee; (ii) Selection of Syndicate Members; (iii) Constitution of a task force for due diligence; (iv) Listing; (v) Offering Circular; (vi) Research papers; (vii) Pre-marketing; (viii) Timing, pricing and size of the issue; (ix) Roadshows; (x) Book building and pricing of the issue; (xi) Closing of the issue; (xii) Allotment; (xiii) Investor Relation Programme; and (xiv) Quarterly Statement.

Constitution of a Board Sub-Committee

To launch a Euro-issue, the issuing company has to take a large number of decisions in time. These decisions normally fall within the power of Board of Directors. It is usually difficult to call Board Meetings frequently and to ensure presence of adequate Board Members. Thus, it is normally advisable to constitute a sub-committee of the Board with full delegation of powers with regard to Euro-issue. The delegation of powers to the Board sub-committee should normally include the following:

- Appointment of agencies;
- Authority to make applications for seeking various approvals;
- Authority to finalise and execute documents and agreements;
- Decisions about the timing, size and pricing of the issue; and
- Allotment of shares.

Selection of Syndicate Members

The success of any Euro-issue depends upon the well planned and coordinated efforts of the syndicate members and the company. The selection of the Syndicate members should be made depending upon the strength and capabilities of each member in different areas of specialisation such as marketing, financial research, distribution etc. The lead manager may be entrusted with the work of selection of syndicate members. The lead manager while selecting the above members, in addition to their strength and capability, should also evaluate their standing, image, reputation, infrastructure, past experience in handling Indian Euro-issue, etc.

Constitution of a task force for due diligence

The due diligence is a process in which a team consisting of legal, technical and financial experts of the lead manager meets top executives of the company and visits the sites of the company in order to understand the strengths, weaknesses, problems and opportunities of the company. The team also studies and analyses the balance sheet of the company and its subsidiaries, its financial arrangement with the group, investment pattern and also the future prospects of the company.

It also scrutinise the minutes of the company, various arrangements entered into by the company with regard to marketing, purchase, technology, ancillary units, employment, etc. and analyse the impact of litigations on the profitability of the company.

The purpose of above exercise is to draft the offering circular (prospectus) and work out marketing strategies for the Euro-issue.

Listing

One of the conditions of Euro-issues is that the securities are to be listed on one or more Overseas Stock Exchanges. The issuing company has to fulfill all the requirements particularly disclosure and documentation as prescribed by the Overseas Stock Exchanges. The company shall take the help of the listing agent in getting its Euro-issue instruments listed on the Overseas Stock Exchanges.

The issuing company shall prepare the requisite documents as prescribed by the Overseas Stock exchange authorities and submit the same along with application to it after scrutinizing the application and obtain the formal listing approval shall be issued by the Overseas Stock Exchange.

The underlying shares against GDRs are to be listed on one or more Indian Stock Exchange(s) on which the company's existing shares are already listed. For this purpose, the company has to apply to the stock exchange authorities to get the shares represented by GDRs listed on the Indian Stock Exchanges. Trading of such shares on Indian Stock Exchange(s) will not commence until the period specified in the guidelines after the date of issue of the GDRs.

Offering Circular

Offering Circular is a mirror through which the prospective investors can access vital information regarding the company in order to form their investment strategies.

It is to be prepared very carefully giving true and complete information regarding the financial strength of the company, its past performance, past and envisaged research and business promotion activities, track record of promoters and the company, ability to trade the securities on Euro capital market.

The Offering Circular should be very comprehensive to take care of overall interests of the prospective investor. The Offering Circular for Euro-issue offering should typically cover the following contents:

- (i) Background of the company and its promoters including date of incorporation and objects, past performance, production, sales and distribution network, future plans, etc.
- (ii) Capital structure of the company-existing, proposed and consolidated.
- (iii) Deployment of issue proceeds.
- (iv) Financial data indicating track record of consistent profitability of the company.
- (v) Group investments and their performance including subsidiaries, joint venture in India and abroad.
- (vi) Investment considerations.
- (vii) Description of shares.
- (viii) Terms and conditions of global depository receipt and any other instrument issued along with it.
- (ix) Economic and regulatory policies of the Government of India.
- (x) Details of Indian securities market indicating stock exchange, listing requirements, foreign investments in Indian securities.
- (xi) Market price of securities.
- (xii) Dividend and capitalisation.
- (xiii) Securities regulations and exchange control.
- (xiv) Tax aspects indicating analysis of tax consequences under Indian law of acquisition, membership and sale of shares, treatment of capital gains tax, etc.
- (xv) Status of approvals required to be obtained from Government of India.
- (xvi) Summary of significant differences in Indian GAAP, UK GAAP and US GAAP and expert's opinion.
- (xvii) Report of statutory auditor.
- (xviii) Subscription and sale.
- (xix) Transfer restrictions in respect of instruments.
- (xx) Legal matters etc.
- (xxi) Other general information not forming part of any of the above.

A copy of the Offering Circular is required to be sent to the Registrar of Companies, the SEBI and the Indian Stock Exchanges for record purposes.

Research Papers

Research analysts team of lead manager/co-lead manager prepares research papers on the company before the issue. These papers are very important marketing tools as the international investors normally depend a lot on the information provided by the research analysts for making investment decisions.

Pre-marketing

Pre-marketing exercise is a tool through which the syndicate members evaluate the prospects of the issue. This

is normally done closer to the issue. The research analysts along with the sales force of the syndicate members meet the prospective investors during pre-marketing roadshows. This enables the syndicate members to understand the market and the probable response from the prospective investors. The pre-marketing exercise helps in assessing the depth of investors' interest in the proposed issue, their view about the valuation of the share and the geographical locations of the investors who are interested in the issue. The response received during pre-marketing provides vital information for taking important decisions relating to timing, pricing and size of the issue. This would also help the syndicate members in evolving strategies for marketing the issue.

Timing, pricing and size of the Issue

After pre-marketing exercise, the important decisions of timing, pricing and size of the issue are taken. The proper time of launching the issue is when the fundamentals of the company and the industry are strong and the market price of the shares are performing well at Indian Stock Exchanges. The timing should also not clash with some other major issues of the Indian as well as other country companies. The decision regarding the size of issue is inversely linked with the pricing i.e. larger the size, the comparatively lower the price or vice-versa.

Roadshows

Roadshows represent meetings of issuers, analysts and potential investors. Details about the company are presented in the roadshows and such details usually include the following information about the company making the issue:

- History
- Organisational structure
- Principal objects
- Business lines
- Position of the company in Indian and international market
- Past performance of the company
- Future plans of the company
- Competition - domestic as well as foreign
- Financial results and operating performance
- Valuation of shares
- Review of Indian stock market and economic situations.

Thus at road shows, series of information presentations are organised in selected cities around the world with analysts and potential institutional investors. It is, in fact, a conference by the issuer with the prospective investors.

Road show is arranged by the lead manager by sending invitation to all prospective investors.

Book building and pricing of the Issue

During road shows, the investors give indication of their willingness to buy a particular quantity at particular terms. Their willingness is booked as orders by the marketing force of lead manager and co-lead manager. This process is known as book building.

Price is a very critical element in the market mix of any product or service. This is more so in case of financial assets like stocks and bonds and specially in case of Euro issues. The market price abroad has a strong correlation to the near future earnings potential, fundamentals governing industry and the basic economic state of the country. Several other factors like prevalent practices, investor sentiment, behaviour towards issues of a particular country, domestic market process etc., are also considered in determination of issue price. Other factors such as the credit rating of the country, interest rate and the availability of an exit route are important.

Closing of the Issue and Allotment

Closing is essentially an activity confirming completion of all legal documentation and formalities based on which the company issues the share certificate to the depository and deposits the same with the domestic custodian. Once the issue is closed and all legal formalities are over, the allotment is finalised. Thereafter, the company issues shares in favour of the Overseas Depository Bank and deposits the same with the domestic custodian for custody. The particulars of the Overseas Depository Bank are required to be entered into the Register of Members of the company.

Investor Relation Programme

The international investors expect that the issuing company maintains contact with them after the issue. These investors always like to be informed by the company about the latest developments, the performance of the company, the factors affecting performance and the company's plans. It is, therefore, essential for the GDR issuing company to set up an investor relation programme. Good investor relation ensures goodwill towards the company and it would help the company in future fund raising efforts.

FOREIGN CURRENCY EXCHANGEABLE BONDS

Issue of Foreign Currency Exchangeable Bonds (FCEB) are regulated by Foreign Currency Exchangeable Bonds Scheme, 2008 issued by Ministry of Finance, Department of Economic Affairs.

What is FCEB?

- (i) a bond expressed in foreign currency.
- (ii) the principal and the interest in respect of which is payable in foreign currency.
- (iii) issued by an issuing company, being an Indian company.
- (iv) subscribed by a person resident outside India.
- (v) Exchangeable into equity shares of another company, being offered company which is an Indian company.
- (vi) Either wholly or partly or on the basis of any equity related warrants attached to debt instruments.

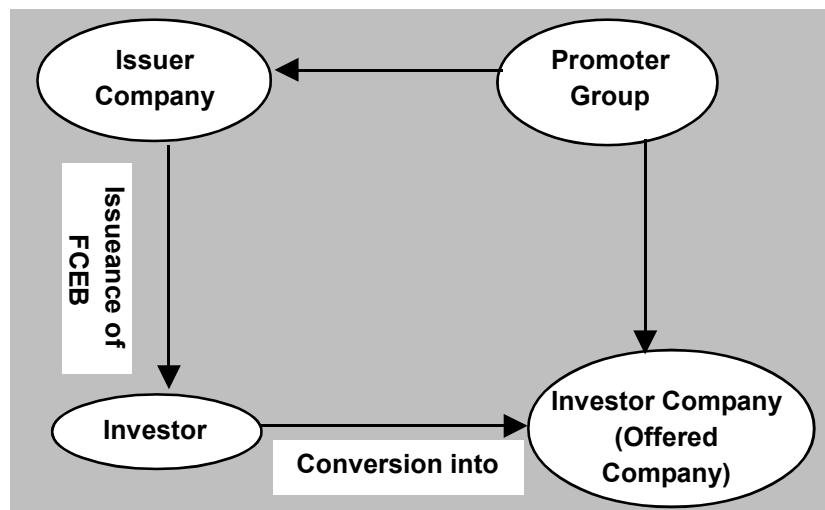
It may be noted that issuing company to be the part of promoter group of offered company and the offered company is to be listed and is to be eligible to receive foreign investment.

The launch of the Foreign Currency Exchangeable Bonds (FCEB) scheme affords a unique opportunity for Indian promoters to unlock value in group companies. FCEBs are another arrow in the quiver of Indian promoters to raise money overseas to fund their new projects and acquisitions, both Indian and global, by leveraging a part their shareholding in listed group entities.

An FCEB involves three parties –

- (i) The issuer company (issuer),
- (ii) The offered company (OC) and
- (iii) Investor.

Under this option, an issuer company may issue FCEBs in foreign currency, and these FCEBs are convertible into shares of another company (offered company) that forms part of the same promoter group as the issuer company. For example, company ABC Ltd. issues FCEBs, then the FCEBs will be convertible into shares of company XYZ Ltd. that are held by company ABC Ltd. and where companies ABC Ltd. and XYZ Ltd. form part of the same promoter group. Unlike FCCBs that convert into shares of issuer itself, FCEBs are exchangeable into shares of OC. Also, relatively, FCEB has an inherent advantage that it does not result in dilution of shareholding at the OC level.



DIFFERENCE BETWEEN FCCB AND FCEB

The essential difference between an FCCB and FCEB lies in their convertibility whereby in the case of an FCCB offering, the bonds convert into shares of the company that issued the bonds, while in the case of an FCEB offering, the bonds are convertible into shares not of the issuer company, but that of another company forming part of its group.

ISSUE OF FOREIGN CURRENCY EXCHANGEABLE BONDS (FCEB) SCHEME, 2008

In Financial Year 2007-08, the Indian Government notified the Foreign Currency Exchangeable Bonds Scheme, 2008 for the issue of FCEBs. The provisions of the scheme is as under:

Eligible Issuer: The Issuing Company shall be part of the promoter group of the Offered Company and shall hold the equity share/s being offered at the time of issuance of FCEB.

Offered Company: The Offered Company shall be a listed company, which is engaged in a sector eligible to receive Foreign Direct Investment (FDI) and eligible to issue or avail of Foreign Currency Convertible Bond (FCCB) or External Commercial Borrowings (ECB).

Entities not eligible to issue FCEB: An Indian company, which is not eligible to raise funds from the Indian securities market, including a company which has been restrained from accessing the securities market by the SEBI shall not be eligible to issue FCEB.

Eligible subscriber: Entities complying with the FDI policy and adhering to the sectoral caps at the time of issue of FCEB can subscribe to FCEB. Prior approval of the Foreign Investment Promotion Board (FIPB), wherever required under the FDI policy, should be obtained.

Entities not eligible to subscribe to FCEB: Entities prohibited to buy, sell or deal in securities by the SEBI will not be eligible to subscribe to FCEB.

End-use of FCEB proceeds

End-use of FCEB proceeds	End-uses not permitted
<p>Issuing Company :</p> <p>(i) The proceeds of FCEB may be invested by the issuing company overseas by way of direct investment including in Joint Ventures or Wholly Owned Subsidiaries abroad, subject to the existing guidelines on overseas investment in Joint Ventures / Wholly Owned Subsidiaries.</p> <p>(ii) The proceeds of FCEB may be invested by the issuing company in the promoter group companies.</p>	<p>All-in-cost</p> <p>The rate of interest payable on FCEB and the issue expenses incurred in foreign currency shall be within the all-in-cost ceiling as specified by RBI under the ECB policy.</p>
<p>Promoter Group Companies :</p> <p>Promoter group companies receiving investments out of the FCEB proceeds may utilize the amount in accordance with end-uses prescribed under the ECB policy.</p>	<p>Pricing of FCEB</p> <p>At the time of issuance of FCEB the exchange price of the offered listed equity shares shall not be less than the higher of the following two:</p> <p>(i) The average of the weekly high and low of the closing prices of the shares of the offered company quoted on the stock exchange during the six months preceding the relevant date; and</p> <p>(ii) The average of the weekly high and low of the closing prices of the shares of the offered company quoted on a stock exchange during the two week preceding the relevant date.</p>
	<p>Average Maturity</p> <p>Minimum maturity of FCEB shall be five years. The exchange option can be exercised at anytime before redemption. While exercising the exchange option, the holder of the FCEB shall take delivery of the offered shares. Cash (Net) settlement of FCEB shall not be permissible.</p>
	<p>Parking of FCEB proceeds abroad</p> <p>The proceeds of FCEB may be retained and / or deployed overseas by the issuing / promoter group companies in accordance with the policy for the ECB or repatriated to India forced it to the borrowers' Rupee accounts with AD Category I banks in India pending utilization for permissible end-uses.</p>
	<p>Operational Procedure</p> <p>Issuance of FCEB shall require prior approval of the Reserve Bank of India under the Approval Route for raising ECB. The Reporting arrangement for FCEB shall be as per the extant ECB policy.</p>

FOREIGN CURRENCY CONVERTIBLE BONDS

The FCCBs are unsecured, carry a fixed rate of interest and an option for conversion into a fixed number of equity shares of the issuer company. Interest and redemption price (if conversion option is not exercised) is payable in dollars. FCCBs shall be denominated in any freely convertible Foreign Currency. However, it must be kept in mind that FCCB issue proceeds need to conform to ECB end use requirements.

Foreign investors also prefer FCCBs because of the dollar denominated servicing, the conversion option and, the arbitrage opportunities presented by conversion of the FCCBs into equity at a discount on prevailing Indian market price.

In addition, 25% of the FCCB proceeds can be used for general corporate restructuring.

The major drawbacks of FCCBs are that the issuing company cannot plan its capital structure as it is not assured of conversion of FCCBs. Moreover, the projections for cash outflow at the time of maturity cannot be made.

Benefits to the Issuer Company

- Being Hybrid instrument, the coupon rate on FCCB is particularly lower than pure debt instrument there by reducing the debt financing cost.
- FCCBs are book value accretive on conversion. It saves risks of immediate equity dilution as in the case of public shares. Unlike debt, FCCB does not require any rating nor any covenant like securities, cover etc.
- It can be raised within a month while pure debt takes a longer period to raise. Because the coupon is low and usually payable at the time of redeeming the instrument, the cost of withholding tax is also lower for FCCBs compared with other ECB instruments.

Benefits to Investors

- It has advantage of both equity and debt.
- It gives the investor much of the upside of investment in equity, and the debt portion protects the downside.
- Assured return on bond in the form of fixed coupon rate payments.
- Ability to take advantage of price appreciation in the stock by means of warrants attached to the bonds, which are activated when price of a stock reaches a certain point.
- Significant Yield to maturity (YTM) is guaranteed at maturity.
- Lower tax liability as compared to pure debt instruments due to lower coupon rate.

FCCB AND ORDINARY SHARES (THROUGH DEPOSITORY RECEIPT MECHANISM) SCHEME, 1993

DEFINITIONS

Domestic Custodian Bank

It means a banking company which acts as a custodian for the ordinary shares or Foreign Currency Convertible Bonds of an Indian Company which are issued by it against Global Depository Receipts or certificates.

Foreign Currency Convertible Bonds

It means bonds issued in accordance with this scheme and subscribed by a non-resident in foreign currency and convertible into ordinary shares of the issuing company in any manner, either in whole, or in part, on the basis of any equity related warrants attached to debt instruments.

Global Depository Receipts

It means any instrument in the form of a Depository receipt or certificate (by whatever name it is called) created by the Overseas Depository Bank outside India and issued to non-resident investors against the issue of ordinary shares or Foreign Currency Convertible Bonds of issuing company.

Issuing Company

It means an Indian Company permitted to issue Foreign Currency Convertible Bonds or ordinary shares of that company against Global Depository Receipts.

Overseas Depository Bank

It means a bank authorised by the issuing company to issue Global Depository Receipts against issue of Foreign Currency Convertible Bonds or ordinary shares of the issuing company.

FCCBs are governed by the 'Issue of Foreign Currency Convertible Bonds and Ordinary Shares (through Depository Receipt Mechanism) Scheme, 1993' as amended from time to time and Notification FEMA No.120/RB-2004 dated July 7, 2004. The issuance of FCCBs was brought under the ECB guidelines in August 2005. In addition to the requirements of (i) having the maturity of the FCCB not less than 5 years, (ii) the call & put option, if any, shall not be exercisable prior to 5 years, (iii) issuance of FCCBs only without any warrants attached, (iv) the issue related expenses not exceeding 4% of issue size and in case of private placement, shall not exceed 2% of the issue size, etc. as required in terms of Notification FEMA No. 120/RB-2004 dated July 7, 2004, FCCBs are also subject to all the regulations which are applicable to ECBs.

Redemption of FCCBs

Keeping in view the need to provide a window to facilitate refinancing of FCCBs by the Indian companies which may be facing difficulty in meeting the redemption obligations, Designated AD Category - I banks have been permitted to allow Indian companies to refinance the outstanding FCCBs, under the automatic route, subject to compliance with the terms and conditions set out hereunder:

- (i) Fresh ECBs/ FCCBs shall be raised with the stipulated average maturity period and applicable all-in-cost being as per the extant ECB guidelines;
- (ii) The amount of fresh ECB/FCCB shall not exceed the outstanding redemption value at maturity of the outstanding FCCBs;
- (iii) The fresh ECB/FCCB shall not be raised six months prior to the maturity date of the outstanding FCCBs ;
- (iv) The purpose of ECB/FCCB shall be clearly mentioned as 'Redemption of outstanding FCCBs' in Form 83 at the time of obtaining Loan Registration Number from the Reserve Bank;
- (v) The designated AD - Category I bank should monitor the end-use of funds;
- (vi) ECB / FCCB beyond USD 500 million for the purpose of redemption of the existing FCCB will be considered under the approval route; and
- (vii) ECB / FCCB availed of for the purpose of refinancing the existing outstanding FCCB will be reckoned as part of the limit of USD 750 million available under the automatic route as per the extant norms.

Restructuring of FCCBs involving change in the existing conversion price is not permissible. Proposals for restructuring of FCCBs not involving change in conversion price will, however, be considered under the approval route depending on the merits of the proposal.

EXTERNAL COMMERCIAL BORROWINGS (ECB)

ECBs are commercial loans raised by eligible resident entities from recognised non-resident entities and should conform to parameters such as minimum maturity, permitted and non-permitted end-uses, maximum all-in-cost

ceiling, etc. The parameters apply in totality and not on a standalone basis. The framework for raising loans through ECB comprises the following three tracks:

Track I: Medium term foreign currency denominated ECB with minimum average maturity of 3/5 years.

Track II: Long term foreign currency denominated ECB with minimum average maturity of 10 years.

Track III: Indian Rupee (INR) denominated ECB with minimum average maturity of 3/5 years.

FORMS OF ECB

The ECB Framework enables permitted resident entities to borrow from recognized non-resident entities in the following forms:

1. Loans including bank loans;
2. Securitized instruments (e.g. floating rate notes and fixed rate bonds, non-convertible, optionally convertible or partially convertible preference shares / debentures);
3. Buyers' credit;
4. Suppliers' credit;
5. Foreign Currency Convertible Bonds (FCCBs);
6. Financial Lease; and
7. Foreign Currency Exchangeable Bonds (FCEBs)

However, ECB framework is not applicable in respect of the investment in Non-convertible Debentures (NCDs) in India made by Registered Foreign Portfolio Investors (RFPIs)

The ECBs are classified under three 'Tracks' under the new framework:

Track I (ECB in FCY over 3/5 average maturity)	Track II (ECB in FCY over 10 years average maturity)	Track III (ECB in INK)
Minimum Average Maturity		
<ul style="list-style-type: none"> Up to USD 50 mn (earlier, USD 20 mn): 3 years Beyond USD 50 mn: 5 years 5 years for eligible borrowers irrespective of the amount of borrowing. 5 years for FCCB/FCEBs irrespective of the amount of borrowing. The call and put option, if any, for FCCBs shall not be exercisable prior to 5 years. 	10 years, irrespective of amount	<ul style="list-style-type: none"> Same as Track I
Eligible Borrowers		
<ul style="list-style-type: none"> Companies in following sectors: <ul style="list-style-type: none"> o Manufacturing sector o Software development 	<ul style="list-style-type: none"> All entities under Track I Companies in infrastructure sector (definition aligned with 	<ul style="list-style-type: none"> All entities listed under Track II All NBFCs coming under the regulatory purview of the RBI

<ul style="list-style-type: none"> o Shipping and airlines companies • Units in SEZs • Small Industries and Development Bank of India • Exim Bank (approval route) • Companies in infrastructure sector, NBFCs–IFCs, NBFCs – Assets Finance companies, Holding companies and core Investment Companies(CICs) 	<p>Harmonised Master List of Government of India)</p> <ul style="list-style-type: none"> • Holding companies • Core investment companies • REITs and INVTs registered with SEBI 	<ul style="list-style-type: none"> • Entities engaged in micro finance activities, subject to conditions • Companies in Miscellaneous Services, viz. <ul style="list-style-type: none"> o R&D o Training (excluding educational institutes) o Companies supporting infrastructure o Logistic services • SEZs/NMIZs Developers
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Exchange Commercial Borrowings (ECB) Policy - Revised Framework published vide A.P. (DIR Series) Circular No. 32 dated 30th November 2015

Recognised lenders		
<ul style="list-style-type: none"> • International banks • International capital market: • Multilateral financial institutions/ regional financial institutions and government owned financial institutions • Export credit agencies • Suppliers of equipment • Foreign equity holders • Overseas long-term Investors such as: <ul style="list-style-type: none"> – prudentially regulated financial entities – Pension funds – Insurance companies – Sovereign Wealth Funds – Financial institutions located International Financial Services Centres in India • Overseas branches/subsidiaries of Indian bank 	<ul style="list-style-type: none"> • All entities listed under Track I but for overseas branches/ subsidiaries of Indian bank. 	<ul style="list-style-type: none"> • All entities listed under Track I but for overseas branches/ subsidiaries of Indian banks. • In case of NBFCs-MFIs, other eligible MFIs not for profit companies and NGOs, ECB can also be availed from overseas organisation and individual satisfying prescribed conditions.
All-in-Cost Ceiling (AIC)		
<ul style="list-style-type: none"> • Average maturity of 3-5 years: 300 bps over the 6-month LIBOR • Average maturity of above 5 years: 450 bps over the 6-month LIBOR • Penal interest: Maximum 2% over and above contracted interest rate 	<ul style="list-style-type: none"> • Maximum spread of 500 bps per annum over the benchmark has been prescribed. 	<ul style="list-style-type: none"> • In line with the market conditions

Permitted end-users:		
<ul style="list-style-type: none"> • Capital expenditure in the form of : <ul style="list-style-type: none"> o Import of capital goods; (including for services; technical know-how and license fees, provided they are part of these capital goods) o Local sourcing of capital goods: o New projects o Modernisation/expansion of existing units o Investment in joint ventures (JV)/wholly-owned subsidiaries (WOS) overseas o Acquisition of shares of PSUs under the disinvestment programme of Government of India o Refinancing of existing trade credit raised for import of capital goods o Payment of capital goods already shipped/imported not unpaid; o Refinancing of existing ECB, provided residual maturity is not reduced. • SIDBI - only for the purpose of onlending to borrowers in the MSME sector, • Units of SEZs - only for their ovvn requirements, • Shipping and airlines companies - only for import of vesels and aircrafts respectively • For general corporate purpose (including Wvorking capital), provided the ECB is raised from direct/indirect equity holder or from a group company; for a minimum average maturity of 5 years, • NBFC–IFCs and NBFCs–AFCs can raise ECB only for financing infrastructure. • Holding Companies and CICs shall use ECB proceeds only for 	<ul style="list-style-type: none"> • Any end-use other than the following: <ul style="list-style-type: none"> o Real estate activiities o Investing in capital market o Using proceeds for equity investment domestically o On-lending to other entries with any of the above objective; o Purchase of land 	<ul style="list-style-type: none"> • Any end-use other than the following : <ul style="list-style-type: none"> o Real estate activities o Investing in capital market o Using the proceeds for equity investment domestically o On-lending to other entities with any of the above objectives o Purchase of land • SEZs/NMIZs Developers Only for providing infrastructure facilities within SEZ/NMIZ • NBFCs can use ECB proceeds for: <ul style="list-style-type: none"> o On-lending for any activities including infrastructure sector as permitted by the concerned regulatory department of RBI o Hypothecated loans to domestic entities for acquisition of capital goods/ equipment o Providing capital goods/ equipment to domestic entities by way of lease/ hire-purchase • Entities in micro-finance sector – Only for on-lending to self-help groups or for micro-credit or for bona fide micro-finance activity including capacity building.

on-lending to infrastructure special purpose vehicles (SPVs) <ul style="list-style-type: none"> • ECBs under the approval route: <ul style="list-style-type: none"> o Import of second-hand good; as per DGFT guidelines o On-lending by Exim Bank 		
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Other Key Features

Individual Units

Sector	Route	
	<i>Automatic</i>	<i>Approval</i>
Infrastructure and manufacturing NBFC–IFCs, NBFCs–AFCs, Holding Companies and Core Investment Companies	Upto USD 750 million	USD 750 million and above
Software development sector	Upto USD 200 million	USD 200 million and above
Micro finance activities	Upto USD 100 million	USD 100 million and above
Others	Upto USD 500 million	USD 500 million and above

- Above-mentioned limits are separate from the limits allowed under the framework for issuance of rupee denominated bonds overseas
- For computation of individual limits under Track III, exchange rate prevailing on the date of agreement should be taken into account.

Currency of Borrowing

- ECB can be raised in any freely convertible currency as well as in INR.
- For INR-denominated ECB, lenders (other than foreign equity holders) are required to mobilise INR through swaps/outright sale undertaken through an AD Category I bank in India.
- Change of currency from one convertible foreign currency to another convertible foreign currency/INR is freely permitted.
- Rate for conversion into INR: the rate prevailing on the date of agreement for such change or any exchange rate lower than the rate prevailing on the date of agreement.
- Change of currency from INR to foreign currency is not permitted.

Hedging requirement

Eligible Borrowers shall have a board approved risk management policy and shall keep their ECB exposure hedged 100% at all times. Further, the designated AD Category-I bank shall verify that 100% hedging requirement is complied with during the currency of ECB and report the position to RBI through ECB 2 returns. Also, the entities raising ECB under the provisions of tracks I and II are required to follow the guidelines for hedging issued, if any, by the concerned sectoral or prudential regulator in respect of foreign currency exposure.

Operational aspects on hedging:

Wherever hedging has been mandated by the RBI, the following should be ensured:

- i. **Coverage:** The ECB borrower will be required to cover principal as well as coupon through financial hedges. The financial hedge for all exposures on account of ECB should start from the time of each such exposure (i.e. the day liability is created in the books of the borrower).
- ii. **Tenor and rollover:** A minimum tenor of one year of financial hedge would be required with periodic rollover duly ensuring that the exposure on account of ECB is not unhedged at any point during the currency of ECB.
- iii. **Natural Hedge:** Natural hedge, in lieu of financial hedge, will be considered only to the extent of offsetting projected cash flows / revenues in matching currency, net of all other projected outflows. For this purpose, an ECB may be considered naturally hedged if the offsetting exposure has the maturity/cash flow within the same accounting year. Any other arrangements/ structures, where revenues are indexed to foreign currency will not be considered as natural hedge.

Conversion of ECB into equity

Conversion of ECBs into equity is permitted (including those which are matured but unpaid) subject to the following conditions:

- The activity of the borrowing company is covered under the automatic route or approval route, wherever applicable, for foreign equity participation has been obtained as per the extant FDI policy;
- The conversion, which should be with the lender's consent and without any additional cost, will not result in breach of applicable sector cap on the foreign equity holding;
- Applicable pricing guidelines for shares are complied with;
- Reporting requirements are fulfilled;
- If the borrower concerned has availed of other credit facilities from the Indian banking system, including overseas branches/subsidiaries, the applicable prudential guidelines issued by the Department of Banking Regulation of RBI, including guidelines on restructuring are complied with; and
- Consent of other lenders, if any, to the same borrower is available or atleast information regarding conversions is exchanged with other lenders of the borrower.

Debt Equity Ratio

The borrowing entities will be governed by the guidelines on debt equity ratio issued, if any, by the sectoral or prudential regulator concerned.

Parking of Proceeds

(i) Parking of ECB proceeds abroad: ECB proceeds meant only for foreign currency expenditure can be parked abroad pending utilization. Till utilisation, these funds can be invested in the liquid assets:

(ii) Parking of ECB proceeds domestically: ECB proceeds meant for Rupee expenditure should be repatriated immediately for credit to their Rupee accounts with AD Category I banks in India. ECB borrowers are also allowed to park ECB proceeds in term deposits with AD Category I banks in India for a maximum period of 12 months. These term deposits should be kept in unencumbered position.

Liquid Assets includes :

- a) deposits or Certificate of Deposit or other products offered by banks rated not less than AA (-) by Standard and Poor/ Fitch IBCA or Aa3 by Moody's;
- b) Treasury bills and other monetary instruments of one year maturity having minimum rating as indicated above; and
- c) deposits with overseas branches/ subsidiaries of Indian banks abroad.

Prepayment of ECB

Pre-payment is permitted without any restriction on amount subject to compliance with stipulated minimum average maturity.

Change of designated AD bank

Change of designated AD Bank is permitted, subject to NOC from existing AD bank (without any requirement of undertaking any due diligence).

Dissemination of ECB Information

ECB details such as name of the borrower, amount, purpose and maturity under automatic/ approval routes would be put up on RBI's website on a monthly basis.

Security for raising ECB

AD Category I banks are permitted to allow creation of charge on immovable assets, movable assets, financial securities and issue of corporate and/ or personal guarantees in favour of overseas lender / security trustee, to secure the ECB to be raised / raised by the borrower, subject to satisfying themselves that:

- (i) the underlying ECB is in compliance with the extant ECB guidelines;
- (ii) there exists a security clause in the Loan Agreement requiring the ECB borrower to create charge, in favour of overseas lender / security trustee, on immovable assets / movable assets / financial securities/ issuance of corporate and / or personal guarantee; and
- (iii) No objection certificate, as applicable, from the existing lenders in India has been obtained.

Once aforesaid conditions are met, the AD Category I bank may permit creation of charge on immovable assets, movable assets, financial securities and issue of corporate and / or personal guarantees, during the currency of the ECB with security co-terminating with underlying ECB.

Reporting Requirements

Borrowings under ECB Framework are subject to reporting requirements in respect of the following:

- (i) **Loan Registration Number (LRN):** Any draw-down in respect of an ECB as well as payment of any fees / charges for raising an ECB should happen only after obtaining the LRN from RBI.
- (ii) **Changes in terms and conditions of ECB:** Permitted changes in ECB parameters should be reported to the Department of Statistics and Information Management (DSIM) through revised Form 83 at the earliest, in any case not later than 7 days from the changes effected. While submitting revised Form 83 the changes should be specifically mentioned in the communication.
- (iii) **Reporting of actual transactions:** The borrowers are required to report actual ECB transactions through ECB 2 Return through the AD Category I bank on monthly basis so as to reach DSIM within seven working days from the close of month to which it relates. Changes, if any, in ECB parameters should also be incorporated in ECB 2 Return.

Transitional Provisions

The new framework will come into force from the date of publication in the Official Gazette, of the relative regulations issued under FEMA. The same will be reviewed after one year, based on experience and evolving macro-economic situation.

ECB can be raised under existing framework up to 31 March 2016, provided the loan agreement is signed before the commencement of the revised framework.

Further, in following cases, ECB can be raised under existing framework, provided loan agreement is signed and LRN is obtained by 31 March 2016:

- ECB for working capital by airline companies
- ECB for consistent foreign exchange earners under USD 10 billion Scheme.

LESSON ROUND UP

- Indian companies are allowed to raise equity capital in the international market through the issue of GDR/ADR/FCCB/FCEB.
- In the Year 2007-2008, the Indian Government notified the Foreign Currency Exchangeable Bonds Scheme, 2008 for the issue of FCEBs.
- FCCB are regulated by the FCCB and Ordinary Shares (through Depository Receipt Mechanism) Scheme, 1993.
- The FCCBs are unsecured, carry a fixed rate of interest and an option for conversion into a fixed number of equity shares of the issuer company.
- The issue of GDRs/FCCBs requires the approval of a Board of Directors, shareholders, "In principle and Final" approval of Ministry of Finance, Approval of Reserve Bank of India, In-principle consent of Stock Exchange for listing of underlying shares and In-principle consent of Financial institutions.
- External Commercial Borrowings (ECB) include commercial bank loans, buyers' credit, suppliers credit, securitised instruments such as floating rate notes and fixed rate bonds.
- External Commercial Borrowings (ECB) can be accessed under two routes, viz., (i) Automatic Route and (ii) Approval Route.

GLOSSARY

CEDEL	One of the two major organizations in the Eurobond market which clears or handles the physical exchange of, securities and stores securities. Based in Luxembourg, the company is owned by several shareholding banks and operates through a network of agents.
Eurobond	Eurobonds are issued in a specific currency outside the currency's domicile. They are not subject to withholding tax and fall outside the jurisdiction of any one country. The Eurobond market is based in London. Not to be confused with euro-denominated bonds.
Renminbi (RMB)	It is the official currency of China. The primary unit of renminbi is the yuan.
Bridge Finance	Bridging finance is a short-term loan that allows the borrower a period to time, before refinancing the loan. That is, it provides a 'bridge' for the borrower.
DTAA	DTAA or Double Taxation Avoidance Agreement is a tax treaty that India has with other countries. In plain language, what this means for an NRI is, if he/she is a resident in any of those countries and is paying taxes on the income earned in that country, then he/she is eligible for a lower deduction of tax on income earned in India in that financial year.

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation.)

1. What is FCCB? Briefly explain the benefits available to the investors by investing in FCCB.
2. What do you mean by FCEB? What are the eligibility conditions for issuing FCEB?
3. Differentiate between FCCB and FCEB?
4. Describe the procedure for accessing External Commercial Borrowing through approval route?
5. Write short notes on
 - (a) Sponsored ADR/GDR issue
 - (b) Two Way Fungibility Scheme
6. What are the provisions relating to transfer/redemption of GDRs?
7. Who are eligible to access ECBs through automatic route?
8. What are the eligibility conditions for issuing of DPs.
9. Explain the procedure for the issue of Depository Receipts.

This image shows a blank sheet of white paper designed for writing. At the very top, there is a thick, solid black horizontal bar. Below this bar, the page is filled with evenly spaced, thin grey horizontal lines that run across the entire width of the page, providing a guide for letter height and placement. The lines are consistent in color and thickness throughout the document.

Lesson 11

Indian Depository Receipts

LESSON OUTLINE

- Introduction
- Advantages of IDRs
- Regulatory Framework of IDRs- An overview
- Rule 13 of the Companies (Registration of Foreign Companies) Rules, 2014
- SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009
- Rights Issue of Indian Depository Receipts
- Compliances under SEBI (Listing Obligations and Disclosures Requirements) Regulations, 2015
- LESSON ROUND-UP
- GLOSSARY
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

Investment in Indian Depository Receipts (IDRs) is an interesting opportunity for the Indian Investors who are looking for investing their funds in foreign equity. Just like American Depository Receipts or Global Depository Receipts, which are instruments used by Indian Companies to raise money abroad, IDRs are meant for foreign companies looking to raise capital in India.

Indian Depository Receipts means any instrument in the form of a depository receipts created by Domestic Depository in India against the underlying equity shares of issuing company which is located outside India. The Indian IDR holder would thus indirectly own the equity shares of overseas issuer company. IDRs are to be listed and denominated in Indian Currency. An issuing company cannot raise funds in India by issuing IDRs unless it has obtained prior permission from SEBI.

This lesson will enable the students to understand the basic concepts of Indian Depository Receipts (IDRs), Overview of legal framework governing IDRs, Procedures for making an issue of Indian Depository Receipts and Listing compliances required for issuance of Indian Depository Receipts under SEBI (Listing Obligations and Disclosures Requirements) Regulations, 2015.

INTRODUCTION

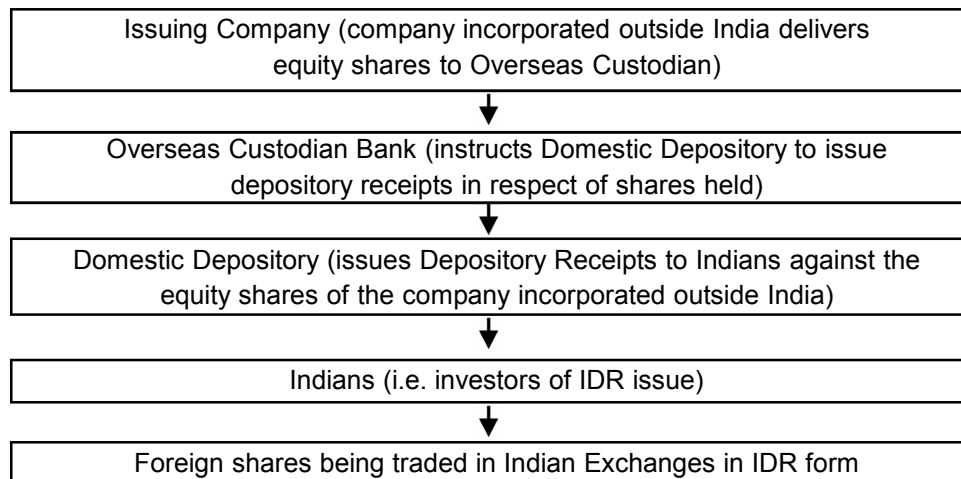
The world has become global village due to the technology advancement and as a result the Securities Market have become international. Companies that previously had to raise capital in the domestic market can now tap foreign sources of capital through ADR/GDR/FCCB/FCEB in overseas market to raise fund from international market. As India is a preferred investment destination among international investors, the Government of India has introduced the concept of Indian Depository Receipts (IDRs) to facilitate listing by foreign companies on Indian Stock Exchanges. Global banking giant Standard Chartered PLC came out with the first issue of IDR and listed itself on the Indian stock exchanges in the year 2010. The IDR issue by Standard Chartered PLC was not only the first IDR offering but it was also the first public offering to complete listing and trading within the reduced timelines of 12 working days as notified by SEBI vide its circular dated April 22, 2010.

Indian Depository Receipt means any instrument in the form of a depository receipt created by Domestic Depository in India against the underlying equity shares of issuing company. "Domestic Depository" means custodian of securities registered with SEBI and authorised by the issuing company to issue Indian Depository Receipts.

Overseas Custodian Bank means a banking company which is established in a country outside India and has a place of business in India and acts as custodian for the equity shares of issuing company against which IDRs are proposed to be issued by having a custodial arrangement or agreement with the Domestic Depository or by establishing a place of business in India.

Process involved in issue of India Depository Receipts (IDRs)

The following flow chart describes the IDRs process :



ADVANTAGES OF IDR

Benefits to the Issuing Company

- It provides access to a large pool of capital to the issuing company.
- It gives brand recognition in India to the issuing company.
- It facilitates acquisitions in India.
- Provides an exit route for existing shareholders.

Benefits to Investors

- It provides portfolio diversification to the investor.
- It gives the facility of ease of investment.
- There is no need to know your customer norms.
- No resident Indian individual can hold more than \$200,000 worth of foreign securities purchased per

year as per Indian foreign exchange regulations. However, this will not be applicable for IDRs which gives Indian residents the chance to invest in an Indian listed foreign entity.

REGULATORY FRAMEWORK OF IDRs – AN OVERVIEW

Regulatory Bodies

- The Securities and Exchange Board of India
- The Ministry of Corporate Affairs
- The Reserve Bank of India

Statutes Governing IDRs

- Section 390 of the Companies Act, 2013
- Rule 13 of the Companies (Registration of Foreign Companies) Rules, 2014
- Chapter X & XA of SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009

Date	Issuing authority	Legislation	Effect
December 13, 2000	Ministry of Corporate Affairs, Government of India, (MCA)	Insertion of section 605 A to the Companies Act, 1956	Enabling section to permit foreign companies to issue IDR's as a security to investors in India
February 23, 2004	MCA	IDR Rules	Created Framework for issue of IDR's
April 3, 2006	SEBI	DIP Guidelines	Disclosure requirements for listing IDR's specified
April 3, 2006	SEBI	SEBI Circular SEBI/CFD/DIL/DIP/20/ 2006/3/4 Model Listing Agreement	Provided the model terms and conditions of an agreement between the issuing company and the stock exchanges for listing IDR's on Indian stock exchange
July 11, 2007	MCA	IDR Rules	Relaxation of eligibility criteria for issue of IDR's
November 29, 2007	SEBI	DIP Guidelines	Permitting retail investors to subscribe to IDR's
January 19, 2009 (January 2009 Amendments)	MCA	IDR Rules	<ul style="list-style-type: none"> • Removal of one (1) year lock in for conversion from IDR to Equity Shares • Permitting issue of IDRs to persons other than persons resident in India. • Overseas Custodian Bank need not have a place of business in India.
April 13, 2009	SEBI	Approving proposal in its Board Meeting	Enable a) mutual funds and FIIs to invest in IDRs subject to the Foreign Exchange Management Act, 1999 ("FEMA"); (b) electronic holding of IDRs; and

			(c) issue of IDRs by custodians on behalf of issuers.
June 9, 2009	SEBI	SEBI Circular SEBI/IMD/CIR No. 1/165935/2009 dated June 9, 2009	Clarification for Mutual Funds for investing in IDRs
June 16, 2009	SEBI	SEBI Circular SEBI/CFD/DIL/IDR/1/2009/16/06 dated June 16, 2009	Simplified Model Listing Agreement for Issuing Companies, whose securities market regulators are signatories to the Multilateral Memorandum of Understandings of International Organization of Securities commission
June 19, 2009	SEBI	SEBI (Facilitation of Issuance of Indian Depository Receipts) (Amendment) Regulations, 2009	<ul style="list-style-type: none"> • Permitting FIIs to invest in IDRs; • Enabling electronic holding of IDRs; and • Enabling issue of IDRs by Custodians on behalf of Issuing Company
July 22, 2009	RBI	RBI Circular RBI/2009-10/106 AP (DIR Series) Circular No. 05 dated July 22, 2009	<ul style="list-style-type: none"> • Prior approval required for banking/ finance companies having presence in India • Clarity on procedure for repatriation of IDR proceeds • One year lock-in on redemption of IDRs • Permitting Investment by FIIs / NRIs in IDRs; • Guideline for redemption/ conversion of IDRs.
July 31, 2009	SEBI	SEBI/CFD/DIL/DIP/37/2009/31/07 dated July 31, 2009	<ul style="list-style-type: none"> • Pro rata allotment of IDRs • Audited Financial Statements to be prepared in accordance with Indian GAAP or with the International Financial Reporting Standards or US GAAP, for a period of three (3) financial years immediately preceding the date of prospectus
September 3, 2009	SEBI	SEBI (ICDR) Regulations, 2009	Replace the DIP guidelines in entirety
September 22, 2009	SEBI	Approving proposal in its board meeting	Permitting issue of IDR's to anchor investor
August 28, 2012	RBI	RBI/2012-13/178 AP (DIR Series) Circular No. 19	RBI allowed partial fungibility of Indian Depository Receipts (IDRs) – redemption or conversion of IDRs into underlying equity shares – in a financial year to the extent of 25 per cent of the IDRs originally issued.

March 01, 2013	SEBI	SEBI Circular No. CIR/CFD/6/2013	Broad Guidelines for fungibility of future IDR issuance and the existed listed IDRs.
March 31, 2014	MCA	GSR 266 (E), dated 31-3-2014	Companies (Registration of Foreign Companies) Rules, 2014
April 1, 2014	MCA	Section 390 of the Companies Act, 2013	Offer of Indian Depository Receipts
September 2, 2015	SEBI	SEBI (Listing Obligation and Disclosure Requirements) Regulations, 2015	Obligation of Listed Entity which has listed its Indian Depository Receipts
November 4, 2015	SEBI	SEBI Circular No. CIR/CFD/CMD/9/2015	Format for quarterly holding pattern, disclosure norms for corporate governance report and manner for compliance with two-way fungibility of IDRs.

RULE 13 OF THE COMPANIES (REGISTRATION OF FOREIGN COMPANIES) RULES, 2014

These rules are applicable to those companies incorporated outside India, whether they have or have not, or will or will not, establish any place of business in India.

For the purposes of section 390, no company incorporated or to be incorporated outside India, whether the company has or has not established, or may or may not establish, any place of business in India (hereinafter in this rule called 'issuing company') shall make an issue of Indian Depository Receipts (IDRs) unless such company complies with the conditions mentioned under this rule, in addition to the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009 and any directions issued by the Reserve Bank of India.

ELIGIBILITY FOR ISSUE OF IDRs

Sub-rule 2 stipulates that the issuing company shall not issue IDRs unless –

- its pre-issue paid-up capital and free reserves are at least US\$ 50 million and it has a minimum average market capitalization (during the last three years) in its parent country of at least US\$ 100 million;
- it has been continuously trading on a stock exchange in its parent or home country (the country of incorporation of such company) for at least three immediately preceding years;
- it has a track record of distributable profits in terms of section 123 of the Act, for at least three out of immediately preceding five years;
- it fulfills such other eligibility criteria as may be laid down by the SEBI from time to time in this behalf.

PROCEDURE FOR MAKING AN ISSUE OF IDRs

Sub-rule 3 lays down the procedure for making an issue of IDRs. The issuing company shall follow the following procedure for making an issue of IDRs:

- the issuing company shall, where required, obtain the necessary approvals or exemptions from the appropriate authorities from the country of its incorporation under the relevant laws relating to issue of capital and IDRs.

- (b) issuing company shall obtain prior written approval from SEBI on an application made in this behalf for issue of IDRs along with the issue size.
- (c) an application under clause (b) shall be made to SEBI (along with draft prospectus) at least ninety days prior to the opening date of the IDRs issue, in such form, along with such fee and furnishing such information as may be specified by the SEBI from time to time:

However, the issuing company shall also file with SEBI, through a Merchant Banker, a due diligence report along with the application under clause (b) in the form specified by SEBI.

- (d) SEBI may, within a period of thirty days of receipt of an application under clause (c), call for such further information, and explanations, as it may deem necessary, for disposal of such application and shall dispose the application within a period of thirty days of receipt of further information or explanation.

However, if within a period of sixty days from the date of submission of application or draft prospectus, SEBI specifies any changes to be made in the draft prospectus, the prospectus shall not be filed with SEBI or Registrar of Companies unless such changes have been incorporated therein.

- (e) the issuing company shall on approval being granted by the SEBI to an application under clause (b), pay to the SEBI an issue fee as may be prescribed from time to time by the SEBI.
- (f) the issuing company shall file a prospectus, certified by two authorized signatories of the issuing company, one of whom shall be a whole-time director and other the Chief Financial Officer, stating the particulars of the resolution of the Board by which it was approved with SEBI and Registrar of Companies, New Delhi before such issue.

However, at the time of filing of said prospectus with the Registrar of Companies, New Delhi, a copy of approval granted by SEBI and the statement of fees paid by the Issuing Company to SEBI shall also be attached.

- (g) the prospectus to be filed with SEBI and the Registrar of Companies, New Delhi shall contain the particulars as prescribed in sub-rule (8) and shall be signed by all the whole-time directors of the issuing company, and the Chief Financial Officer.
- (h) the issuing company shall appoint an overseas custodian bank, a Domestic Depository and a Merchant Banker for the purpose of issue of IDRs.
- (i) the issuing company may appoint underwriters registered with SEBI to underwrite the issue of IDRs.
- (j) the issuing company shall deliver the underlying equity shares or cause them to be delivered to an Overseas Custodian Bank and the said bank shall authorize the domestic depository to issue IDRs.
- (k) the issuing company shall obtain in-principle listing permission from one or more stock exchanges having nationwide trading terminals in India.

REGISTRATION OF DOCUMENTS

Sub-rule 4 provides that the Merchant Banker to the issue of IDRs shall deliver for registration the following documents or information to SEBI and Registrar of Companies at New Delhi, namely:-

- (a) instrument constituting or defining the constitution of the issuing company;
- (b) the enactments or provisions having the force of law by or under which the incorporation of the Issuing company was effected, a copy of such provisions attested by an officer of the company be annexed;
- (c) if the issuing company has established place of business in India, address of its principal office in India;
- (d) if the issuing company does not establish a principal place of business in India, an address in India where the said instrument, enactments or provision or copies thereof are available for public inspection, and if these are not in English, a translation thereof certified by a key managerial personnel of the issuing company shall be kept for public inspection;

- (e) a certified copy of the certificate of incorporation of the issuing company in the country in which it is incorporated;
- (f) the copies of the agreements entered into between the issuing company, the overseas custodian bank, the Domestic Depository, which shall *inter alia* specify the rights to be passed on to the IDR holders;
- (g) if any document or any portion thereof required to be filed with SEBI or the Registrar of Companies is not in English language, a translation of that document or portion thereof in English, certified by a key managerial personnel of the company to be correct and attested by an authorized officer of the Embassy or Consulate of that country in India, shall be attached to each copy of the document.

CONDITIONS FOR ISSUE OF PROSPECTUS AND APPLICATION

Sub-rule 5 deals with conditions required to be fulfilled for issue of prospectus which is as under:

- (a) No application form for the securities of the issuing company shall be issued unless the form is accompanied by a memorandum containing the salient features of prospectus in the specified form.
- (b) An application form can be issued without the memorandum as specified in clause (a), if it is issued in connection with an invitation to enter into an underwriting agreement with respect to the IDRs.
- (c) The prospectus for subscription of IDRs of the Issuing company which includes a statement purporting to be made by an expert shall not be circulated, issued or distributed in India or abroad unless a statement that the expert has given his written consent to the issue thereof and has not withdrawn such consent before the delivery of a copy of the prospectus to SEBI and the Registrar of Companies, New Delhi, appears on the prospectus.
- (d) The provisions of the Act shall apply for all liabilities for mis-statements in prospectus or punishment for fraudulently inducing persons to invest money in IDRs.
- (e) The person(s) responsible for issue of the prospectus shall not incur any liability by reason of any non-compliance with or contravention of any provision of this rule, if –
 - (i) as regards any matter not disclosed, he proves that he had no knowledge thereof; or
 - (ii) the contravention arose in respect of such matters which in the opinion of the Central Government or SEBI were not material.

PROCEDURE FOR TRANSFER AND REDEMPTION

Sub-rule 6 narrates the procedure for transfer and redemption of IDRs.

- (a) A holder of IDRs may transfer the IDRs, may ask the Domestic Depository to redeem them or any person may seek reissuance of IDRs by conversion of underlying equity shares, subject to the provisions of the Foreign Exchange Management Act, 1999, the SEBI Act, 1992, or the rules, regulations or guidelines issued under these Acts, or any other law for the time being in force;
- (b) In case of redemption, Domestic Depository shall request the Overseas Custodian Bank to get the corresponding underlying equity shares released in favour of the holder of IDRs for being sold directly on behalf of holder of IDRs, or being transferred in the books of Issuing company in the name of holder of IDRs and a copy of such request shall be sent to the issuing company for information.
- (c) A holder of IDRs may, at any time, nominate a person to whom his IDRs shall vest in the event of his death and Form FC-5 may be used for this purpose.

REPATRIATION

Sub-rule 7 provides for repatriation of issue proceeds of IDRs.

- (a) The repatriation of the proceeds of issue of IDRs shall be subject to laws for the time being in force relating to export of foreign exchange.

- (b) The number of underlying equity shares offered in a financial year through IDR offerings shall not exceed twenty five per cent of the post issue number of equity shares of the company.
- (c) Notwithstanding the denomination of securities of an Issuing company, the IDRs issued by it shall be denominated in Indian Rupees.
- (d) The IDRs issued under this rule shall be listed on the recognized Stock Exchange(s) in India as specified in clause (k) of sub-rule (3) and such IDRs may be purchased, possessed and freely transferred by a person resident in India as defined in section 2(v) of the Foreign Exchange Management Act, 1999, subject to the provisions of the said Act:

However, the IDRs issued by an issuing company may be purchased, possessed and transferred by a person other than a person resident in India if such Issuing company obtains specific approval from Reserve Bank of India in this regard or complies with any policy or guidelines that may be issued by Reserve Bank of India on the subject matter;

- (e) Every issuing company shall comply with such continuous disclosure requirements as may be specified by SEBI in this regard.
- (f) On the receipt of dividend or other corporate action on the IDRs as specified in the agreements between the Issuing company and the Domestic Depository, the Domestic Depository shall distribute them to the IDR holders in proportion to their holdings of IDRs.

DISCLOSURES

Rule 8 prescribes the disclosures of the following particulars are to be specified in the prospectus or letter of offer:—

- (a) General information
 - (i) Name and address of the registered office of the company;
 - (ii) Name and address of the Domestic Depository, the Overseas Custodian Bank with the address of its office in India, the Merchant Banker, the underwriter to the issue and any other intermediary which may be appointed in connection with the issue of IDRs;
 - (iii) Names and addresses of Stock Exchanges where applications are made or proposed to be made for listing of the IDRs;
 - (iv) The provisions relating to punishment for fictitious applications;
 - (v) Statement/declaration for refund of excess subscription;
 - (vi) Declaration about issue of allotment letters/certificates/ IDRs within the stipulated period;
 - (vii) Date of opening of issue;
 - (viii) Date of closing of issue;
 - (ix) Date of earliest closing of the issue;
 - (x) Declaration by the Merchant Banker with regard to adequacy of resources of underwriters to discharge their respective obligations, in case of being required to do so;
 - (xi) A statement by the issuing company that all moneys received out of issue of IDRs shall be transferred to a separate domestic bank account, name and address of the bank and the nature and number of the account to which the amount shall be credited;
 - (xii) The details of proposed utilisation of the proceeds of the IDR issue.

(b) Capital Structure of the Company

Authorised, issued, subscribed and paid-up capital of the issuing company.

(c) Terms of the issue

- (i) Rights of the IDR holders against the underlying securities;
- (ii) Details of availability of prospectus and forms, i.e., date, time, place etc;
- (iii) Amount and mode of payment seeking issue of IDRs; and
- (iv) Any special tax benefits for the issuing company and holders of IDRs in India.

(d) Particulars of Issue

- (i) Objects of the issue;
- (ii) Cost of the Project, if any; and
- (iii) Means of financing the projects, if any including contribution by promoters.

(e) Company, Management and Project

- (i) Main object, history and present business of the company;
- (ii) The promoters or parent group or owner group and their background. However, in case there are no identifiable promoters, the names, addresses and other particulars as may be specified by SEBI of all the persons who hold 5% or more equity share capital of the company shall be disclosed;
- (iii) subsidiaries of the company, if any;
- (iv) particulars of the Management/Board (i.e. Name and complete address(es) of Directors, Manager, Managing Director or other principal officers of the company);
- (v) location of the project, if any;
- (vi) details of plant and machinery, infrastructure facilities, technology etc., where applicable;
- (vii) schedule of implementation of project and progress made so far, if applicable;
- (viii) nature of product(s), consumer(s), industrial users;
- (ix) particulars of legal, financial and other defaults, if any;
- (x) risk factors to the issue as perceived;
- (xi) consent of Merchant Bankers, overseas custodian bank, the domestic depository and all other intermediaries associated with the issue of IDRs; and
- (xii) the information, as may be specified by SEBI, in respect of listing, trading record or history of the Issuing Company on all the stock exchanges, whether situated in its parent country or elsewhere.

(f) Report

- (i) Where the law of a country, in which the Issuing company is incorporated, requires annual statutory audit of the accounts of the Issuing company, a report by the statutory auditor of the Issuing company, in such form as may be prescribed by SEBI on –
 - (A) the audited financial statements of the Issuing Company in respect of three financial years immediately preceding the date of prospectus, and
 - (B) the interim audited financial statements in respect of the period ending on a date which is less than 180 days prior to the date of opening of the issue, if the gap between the ending date of

the latest audited financial statements disclosed under item (A) and the date of opening of issue is more than 180 days.

However, if the gap between such date of latest financial statements and the date of opening of issue is 180 days or less, the requirement under item (B) shall be deemed to be complied with if a statement, as may be specified by SEBI, in respect of changes in the financial position of issuing company for such gap is disclosed in the prospectus.

Further, in case of an issuing company which is a foreign bank incorporated outside India and which is regulated by a member of the Bank for International settlements or a member of the International Organization of Securities Commissions which is a signatory to a Multinational Memorandum of Understanding with India, the requirement in respect of period beginning with last date of period for which the latest audited financial statements are made and the date of opening of issue shall be satisfied, if the relevant financial statements are based on limited review report of such statutory auditor.

- (ii) Where the law of the country, in which the Issuing company is incorporated, does not require annual statutory audit of the accounts of the Issuing company, a report, in such form as may be specified by SEBI, certified by a Chartered Accountant in practice within the meaning of the Chartered Accountants Act, 1949, on –

- (A) the financial statements of the Issuing Company, in particular on the profits and losses for each of the three financial years immediately preceding the date of prospectus and upon the assets and liabilities of the Issuing Company and

- (B) the interim financial statements in respect of the period ending on a date which is less than 180 days prior to the date of opening of the issue have to be included in the report, if the gap between the ending date of the latest financial statements disclosed under item (A) and the date of opening of issue is more than 180 days.

However, if the gap between such date of latest audited financial statements and the date of opening of issue is 180 days or less, the requirement under clause (B) shall be deemed to be complied with if a statement, as may be specified by SEBI, in respect of changes in the financial position of the issuing company for such gap is disclosed in the prospectus.

- (iii) The gap between date of opening of issue and date of reports under the said provisions shall not exceed 120 days.
- (iv) If the proceeds of the IDR issue are used for investing in other body(ies) corporate, then following details should be given:
 - (a) Name and address(es) of the bodies corporate;
 - (b) The reports stated in para (i) & (ii) above in respect of those bodies corporate also.

(g) Other Information

- (i) Minimum subscription for the issue.
- (ii) Fees and expenses payable to the intermediaries involved in the issue of IDRs.
- (iii) the declaration with regard to compliance with the Foreign exchange Management Act, 1999.

(h) Inspection of Documents

The place at which inspection of the offer documents, the financial statements and auditor's report thereof will be allowed during the normal business hours.

Any other information as specified by SEBI or the Income Tax Authorities or the Reserve Bank of India or other regulatory authorities from time to time.

SEBI (ISSUE OF CAPITAL AND DISCLOSURE REQUIREMENTS) REGULATIONS, 2009

APPLICABILITY

The provisions of Chapter X shall apply to an issue of Indian Depository Receipts made in terms of section 390 of the Companies Act, 2013 and Rule 13 of the Companies (Registration of Foreign Companies) Rules, 2014.

IN PRINCIPLE APPROVAL OF RECOGNIZED STOCK EXCHANGE(S)

In case of an initial public offer or an issue of IDRs, the issuer or issuing company shall obtain from all the recognized stock exchange(s) on which the issuer or issuing company, proposes to, get its IDRs listed.

ELIGIBILITY

An issuing company making an issue of IDR shall satisfy the following:

- (a) the issuing company is listed in its home country;
- (b) the issuing company is not prohibited to issue securities by any regulatory body;
- (c) the issuing company has track record of compliance with securities market regulations in its home country.

CONDITIONS FOR ISSUE OF IDR

An issue of IDR shall be subject to the following conditions:

- (a) issue size shall not be less than fifty crore rupees;
- (b) procedure to be followed by each class of applicant for applying shall be mentioned in the prospectus;
- (c) minimum application amount shall be twenty thousand rupees;
- (d) at least fifty per cent of the IDR issued shall be allotted to qualified institutional buyers on proportionate basis;
- (e) the balance fifty per cent may be allocated among the categories of non-institutional investors and retail individual investors including employees at the discretion of the issuer and the manner of allocation shall be disclosed in the prospectus. Allotment to investors within a category shall be on proportionate basis;
However, atleast thirty percent of IDRs being offered in the public issue shall be available for allocation to retail individual investors and in case of under subscription in retail individual investor category. Spillover to the other categories to the extent of under subscription may be permitted.
- (f) at any given time, there shall be only one denomination of IDR of the issuing company.
- (g) the underlying equity shares against which IDR, are issued have been or will be listed in its home country before listing of IDRs in stock exchange(s).
- (h) the underlying shares of IDRs shall rank pari-passu with the existing shares of the same class.

PROVISION RELATED TO MINIMUM SUBSCRIPTION

For non-underwritten issues

- (a) If the issuing company does not receive the minimum subscription of ninety per cent of the offer through offer document on the date of closure of the issue, or if the subscription level falls below ninety per cent after the closure of issue on account of cheques having being returned unpaid or withdrawal of applications, the issuing company shall forthwith refund the entire subscription amount received.

- (b) If the issuing company fails to refund the entire subscription amount within fifteen days from the date of the closure of the issue, it is liable to pay the amount with interest to the subscribers at the rate of fifteen per cent per annum for the period of delay.

For underwritten issues

If the issuing company does not receive the minimum subscription of ninety per cent of the offer through offer document including devolvement of underwriters within sixty days from the date of closure of the issue, the issuing company shall forthwith refund the entire subscription amount received with interest to the subscribers at the rate of fifteen per cent per annum for the period of delay beyond sixty days.

FUNGIBILITY

The IDRs shall be fungible into underlying equity shares of the issuing company in the manner specified by SEBI and RBI from time to time. Partial fungibility of IDRs (i.e. redemption/conversion of IDRs into underlying equity shares) in a financial year to the extent of 25 % of the IDRs originally issued is allowed. All the IDRs shall have partial two-way fungibility.

The partial two-way fungibility means that the IDRs can be converted into underlying equity shares and the underlying equity shares can be converted into IDRs within the available headroom. The headroom for this purpose shall be the number of IDRs originally issued minus the number of IDRs outstanding which is further adjusted for IDRs redeemed into underlying equity shares. SEBI has issued broad guidelines for fungibility of future IDR issuances and the existing listed IDRs.

FILING OF DRAFT PROSPECTUS, DUE DILIGENCE CERTIFICATES, PAYMENT OF FEES AND ISSUE ADVERTISEMENT FOR IDRs

1. The issuing company shall appoint one or more merchant bankers, at least one of which shall be a lead merchant banker and shall also appoint other intermediaries in consultation with the lead merchant banker and shall enter into an agreement with the merchant banker.
2. Where the issue is managed by more than one merchant banker, the rights, obligations and responsibilities, relating inter-alia to disclosures, allotment, refund and underwriting obligations, if any, of each merchant banker shall be predetermined and disclosed in the prospectus.
3. The issuing company shall file a draft prospectus with SEBI through a merchant banker along with the requisite fee, as prescribed in Companies (Issue of Indian Depository Receipts) Rules, 2004.
4. The prospectus filed with SEBI shall also be furnished to SEBI in a soft copy.
5. The lead merchant bankers shall:
 - (a) submit a due diligence certificate in a prescribed format to SEBI along with the draft prospectus.
 - (b) certify that all amendments, suggestions or observations made by SEBI have been incorporated in the prospectus
 - (c) submit a fresh due diligence certificate, at the time of filing the prospectus with the Registrar of the Companies.
 - (d) furnish a certificate, immediately before the opening of the issue, certifying that no corrective action is required on its part.
 - (e) furnish a certificate, after the issue has opened but before it closes for subscription.
6. The issuing company shall make arrangements for mandatory collection centres.
7. The issuing company shall issue an advertisement in one English national daily newspaper with wide

circulation and one Hindi national daily newspaper with wide circulation, soon after receiving final observations, if any, on the publicly filed draft prospectus with SEBI and contain the minimum disclosures as prescribed by SEBI.

DISPLAY OF BID DATA

Agreements with other intermediaries and others :

- The issuing company shall appoint a registrar and transfer agent which has connectivity with all the depositories.
- The issuing company shall enter into an agreement with overseas custodian bank and domestic depository.
- The lead merchant banker, after independently assessing the capability of other intermediaries and others to carry out their obligations, shall advise the issuing company on their appointment.

Display of bid data and issue of allotment letter

The stock exchange(s) offering online bidding system for the book building process shall display on their website, the data pertaining to book built IDR issue from the date of opening of the bids till at least three days after closure of bids. The letter of allotment for the IDRs are issued simultaneously to all allottees and that in the event of it being impossible to issue letters of regret at the same time, a notice to that effect be issued in the media so that it appears on the morning after the letters of allotment have been dispatched.

DISCLOSURES IN PROSPECTUS AND ABRIDGED PROSPECTUS

1. The prospectus shall contain all material disclosures which are true, correct and adequate so as to enable the applicants to take an informed investment decision.
2. Without prejudice to the generality of sub-regulation (1), the prospectus shall contain:
 - (a) the disclosures specified in Schedule to Companies (Issue of Indian Depository Receipts) Rules, 2004; and
 - (b) the disclosures in the manner as specified in these regulations.
3. The abridged prospectus for issue of Indian Depository Receipts shall contain the disclosures as specified by SEBI in these regulations.

POST-ISSUE REPORTS

1. The merchant banker shall submit post-issue reports to SEBI.
2. The post-issue reports shall be submitted as follows:
 - (a) initial post issue report, within three days of closure of the issue;
 - (b) final post issue report, within fifteen days of the date of finalisation of basis of allotment or within fifteen days of refund of money in case of failure of issue.

UNDERSUBSCRIBED ISSUE

In case of undersubscribed issue of IDR, the merchant banker shall furnish information in respect of underwriters who have failed to meet their underwriting devolvement to SEBI.

FINALISATION OF BASIS OF ALLOTMENT

The executive director or managing director of the stock exchange, where the IDR are proposed to be listed,

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 this behalf by SEBI.

RIGHTS ISSUE OF INDIAN DEPOSITORY RECEIPTS

In the light of the Standard Chartered Rights Issue where rights could not be granted to IDR holders, SEBI amended the ICDR regulations, 2009 on September 23, 2011 by inserting a new chapter viz. Chapter XA in the existing regulations, governing the rights issue of Indian Depository Receipts. The chapter provides for the various governing criteria's for a rights issue of IDR such as applicability, eligibility, disclosures etc.

Eligibility

- Issuer should not be in breach of any ongoing material obligations under the IDR Listing Agreement;
- Application to all recognised stock exchanges, where such IDRs are listed, must have been made, for listing of IDRs to be issued by way of rights, before such issue.

Disclosures

Following disclosures shall be made:

- Disclosures as required in the home country of the issuer;
- An additional wrap (addendum to offer document) attached to the offer document.

The Regulations further provide for:

- Disclosures in Abridged Prospectus;
- Disclosures in Addendum to Offer;
- Disclosures in Abridged Letter of offer;
- Dispatch of abridged letter of offer and application form;
- Pre-Issue Advertisement for rights issue.

Fast Track Issue

- The issuer is in compliance with the provisions of deposit agreement and listing agreement for a period of atleast 3 (Three) years immediately preceding the date of filing of the offer document;
- The offer document has been filled and reviewed by the securities regulator in the home country of the issuer;
- There are no pending show-cause notices or prosecutions proceedings against the issuer or its promoter, or whole-time directors on the reference date by SEBI or the regulatory authorities in its home country restricting them from accessing the capital markets; and
- Issuer has redressed at least 95% (Ninety Five per cent) of the complaints received from the IDR holders before the end of 3 (Three) months period preceding the filing of letter of offer.

Other Relevant Provisions

The Regulations further provide that:

- The rights offering must include a right exercisable by the person concerned to renounce the IDRs offered in favour of any other person subject to applicable laws;
- If an issuer withdraws the rights issue after announcing the record date, he is restricted from making an

application for offering of IDRs on a rights basis for a period of 12 (Twelve) months from the said record date;

- A rights issue shall be open for subscription for a period as applicable under the laws of its home country but in no case less than 10 (Ten) days;
- Issuer shall utilize funds raised in relation to the IDRs pursuant to the rights offering only upon completion of the allotment process.

COMPLIANCES UNDER SEBI (LISTING OBLIGATIONS AND DISCLOSURE REQUIREMENTS) REGULATIONS, 2015

Every issuer of an IDR has to comply with the conditions stipulated in Chapter VII of the SEBI (LODR) Regulations, 2015. The provisions of this chapter shall apply to listed entity whose securities market regulators are signatories to the Multilateral Memorandum of Understanding of International Organization of Securities Commission issuing 'Indian Depository Receipts' as defined under Rule 13 of the Companies (Registration of Foreign Companies) Rules, 2014.

Reference	Subject matter	Requirement
Regulation 67	General Obligations of listed entity.	<ul style="list-style-type: none"> • All correspondences filed with the stock exchange(s) and those sent to the IDR Holders shall be in English. • The listed entity shall comply, at all times, with the rules/regulations/laws of the country of origin. • The listed entity shall undertake that the competent Courts, Tribunals and regulatory authorities in India shall have jurisdiction in the event of any dispute, either with the stock exchange or any investor, concerning the Indian Depository Receipts offered or subscribed or bought in India. • The listed entity shall forward, on a continuous basis, any information requested by the stock exchange, in the interest of investors from time to time. • In case of any claim, difference or dispute under the provisions of chapter VII and other provisions of SEBI (LODR) Regulations applicable to the listed entity, the same shall be referred to and decided by arbitration as provided in the bye-laws and regulations of the stock exchange(s).
Regulation 68	Disclosure of material events or information	To promptly inform to the stock exchange(s) of all events which are material, all information which is price sensitive and/or have bearing on performance/operation of the listed entity and the listed entity shall make the disclosures as specified in Part C of Schedule III of these regulations.
Regulation 69	Holding pattern & Shareholding details	<ul style="list-style-type: none"> • To file with the stock exchange the Indian Depository Receipt holding pattern on a quarterly

		<p>basis within fifteen days of end of the quarter.</p> <ul style="list-style-type: none"> To file the following details with the stock exchange as is required to be filed in compliance with the disclosure requirements of the listing authority or stock exchange in its home country or any other jurisdiction where the securities of the listed entity are listed:(a) Shareholding Pattern;(b) Pre and post arrangement share holding pattern and Capital Structure in case of any corporate restructuring like mergers / amalgamations.
Regulation 70	Periodical Financial Results	<ul style="list-style-type: none"> To file periodical financial results with the stock exchange in such manner and within such time and to the extent that it is required to file as per the listing requirements of the home country. The listed entity shall comply with the requirements with respect to preparation and disclosures in financial results as specified in Part B of Schedule IV.
Regulation 71	Annual Report	<ul style="list-style-type: none"> To submit to stock exchange an annual report at the same time as it is disclosed to the security holder in its home country or in other jurisdictions where such securities are listed. The annual report shall contain the following: <ul style="list-style-type: none"> (a) Report of board of directors; (b) Balance Sheet; (c) Profit and Loss Account; (d) Auditors Report; (e) All periodical and special reports (if applicable); (f) Any such other report which is required to be sent to security holders annually. The listed entity shall comply with the requirements with respect to preparation and disclosure in financial results in annual report as specified in Part B of Schedule IV.
Regulation 72	Corporate Governance	<ul style="list-style-type: none"> To submit to stock exchange a comparative analysis of the corporate governance provisions that are applicable in its home country and in the other jurisdictions in which its equity shares are listed along with the compliance of the same vis-à-vis the corporate governance requirements applicable under regulation 17 to regulation 27, to other listed entities.

Regulation 73	Documents and Information to IDR Holder	<ul style="list-style-type: none"> To disclose/send the following documents to IDR holders, at the same time and to the extent that it discloses to security holders in its home country or in other jurisdictions where its securities are listed: <ul style="list-style-type: none"> (a) Soft copies of the annual report to all the IDR holders who have registered their email address(es) for the purpose. (b) Hard copy of the annual report to those IDR holders who request for the same either through domestic depository or Compliance Officer. (c) the pre and post arrangement capital structure and share holding pattern in case of any corporate restructuring like mergers / amalgamations and other schemes.
Regulation 74	Equitable Treatment to IDR Holders.	<ul style="list-style-type: none"> If the listed entity's equity shares or other securities representing equity shares are also listed on the stock exchange(s) in countries other than its home country, it shall ensure that IDR Holders are treated in a manner equitable with security holders in home country. The listed entity shall ensure that for all corporate actions, except those which are not permitted by Indian laws, it shall treat IDR holders in a manner equitable with security holders in the home country. In case of take-over or delisting or buy-back of its equity shares, the listed entity shall, while following the laws applicable in its home country, give equitable treatment to IDR holders vis-à-vis security holder in home country. The listed entity shall ensure protection of interests of IDR holders particularly with respect to all corporate benefits permissible under Indian laws and the laws of its home country and shall address all investor grievances adequately.
Regulation 75	Advertisements in Newspapers.	<ul style="list-style-type: none"> The listed entity shall publish the following information in the newspaper : <ul style="list-style-type: none"> (a) periodical financial results required to be disclosed; (b) Notices given to its IDR Holders by advertisement; The information specified above shall be issued in at one English national daily newspaper

		circulating in the whole or substantially the whole of India and in one Hindi national daily newspaper in India.
Regulation 76	Terms of Indian Depository Receipts	<ul style="list-style-type: none"> • The listed entity shall pay the dividend as per the timeframe applicable in its home country or other jurisdictions where its securities are listed, whichever is earlier, so as to reach the IDR Holders on or before the date fixed for payment of dividend to holders of its equity share or other securities. • The listed entity shall not forfeit unclaimed dividends before the claim becomes barred by law in the home country of the listed entity, as may be applicable, and that such forfeiture, when effected, shall be annulled in appropriate cases. • The Indian Depository Receipts shall have two-way fungibility in the manner specified by the SEBI from time to time.
Regulation 77	Structure of Indian Depository Receipts	<ul style="list-style-type: none"> • The listed entity shall ensure that the underlying shares of IDRs shall rank <i>pari-passu</i> with the existing shares of the same class and the fact of having different classes of shares based on different criteria, if any, shall be disclosed by the listed entity in the annual report. • The listed entity shall not exercise a lien on the fully paid underlying shares, against which the IDRs are issued, and that in respect of partly paid underlying • shares, against which the IDRs are issued and shall also not exercise any lien except in respect of moneys called or payable at a fixed time in respect of such underlying shares. • The listed entity, subject to the requirements under the laws and regulations of its home country, if any amount be paid up in advance of calls on any underlying shares against which the IDRs are issued, shall stipulate that such amount may carry interest but shall not in respect thereof confer a right to dividend or to participate in profits.
Regulation 78	Record Date	<ul style="list-style-type: none"> • The listed entity, where it is required so to do in its home country or other jurisdictions where its securities may be listed, shall fix the record date for the purpose of payment of dividends or distribution of any other corporate benefits to IDR Holders.

Regulation 79	Voting	<ul style="list-style-type: none"> The listed entity shall give notice in advance of at least four working days to the recognised stock exchange(s) of record date specifying the purpose of the record date. The listed entity shall, either directly or through an agent, send out proxy forms to IDR Holders in all cases mentioning that a security holder may vote either for or against each resolution. Voting rights of the IDR Holders shall be exercised in accordance with the depository agreement.
Regulation 80	Delisting of Indian Depository Receipt	<ul style="list-style-type: none"> The listed entity shall, if it decides to delist Indian Depository Receipts, give fair and reasonable treatment to IDR holders. The listed entity shall comply with such norms and conditions for delisting Indian Depository Receipts as specified by the SEBI or stock exchange in this regard. The listed entity shall, in case underlying equity shares are delisted, shall delist and cancel the Indian Depository Receipts.

LESSON ROUND UP

- Indian Depository Receipt means any instrument in the form of a depository receipt created by Domestic Depository in India against the underlying equity shares of issuing company.
- Issue of IDRs is regulated by section 390 of the Companies Act, 2013, Rule 13 of the Companies (Registration of Foreign Companies) Rules, 2014 and Chapter X of SEBI (ICDR) Regulations, 2009.
- SEBI amended the ICDR regulations by inserting a new chapter XA for governing the provisions for Rights Issue of IDRs.
- The IDRs issued should be listed on the recognized Stock Exchange(s) in India as specified and such IDRs may be purchased, possessed and freely transferred by a person resident in India.
- Issuer of an IDR has to comply with the listing conditions stated in the listing agreement for IDRs
- Every issuer of an IDRs has to comply with the conditions prescribed under SEBI (Listing Obligation and Disclosures Requirements) Regulations, 2015.

GLOSSARY

Fungibility	Fungibility of an instrument refers to inter-changeability of such instrument into another. Such fungibility may be one-way fungibility or two-way fungibility.
Deposit Agreement	Agreement entered into between the issuing company and domestic depository.
Home Country	The country where the issuing company is incorporated and listed.

(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation.)

- [illegible]

Lesson 12

Foreign Portfolio Investors

LESSON OUTLINE

- Introduction
- SEBI (Foreign Portfolio Investors) Regulations, 2014
- Registration of Foreign Portfolio Investors
- Approval of Designated Depository Participant
- Investment Conditions and Restrictions
- Offshore Derivative Instruments (ODIs)
- Obligations and Responsibilities of Foreign Portfolio Investors
- Obligations and Responsibilities of Designated Depository Participants
- Procedure for Inspection & Investigation
- Action in Case of Default
- LESSON ROUND UP
- GLOSSARY
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

In order to harmonize the various available routes for foreign portfolio investment in India, the Securities and Exchange Board of India introduced a new class of foreign investors in India known as the Foreign Portfolio Investors ("FPIs").

Any foreign institutional investors or qualified foreign investor who holds a valid certificate of registration shall deemed to be a FPIs.

This lesson is designed to give an overview of Foreign Portfolio Investor. In this lesson the student will be able to understand about the Concept of FPIs, Registration of FPIs, Offshore Derivative Instruments (ODIs), Obligation of FPIs and DDP & Inspection & Investigation etc.

INTRODUCTION

In order to harmonize the various available routes for foreign portfolio investment in India, the Securities and Exchange Board of India ("SEBI") introduced a new class of foreign investors in India known as the Foreign Portfolio Investors ("FPIs"). This class has been formed by merging the existing classes of investors through which portfolio investments were previously made in India namely, the Foreign Institutional Investors ("FIIs"), Qualified Foreign Investors ("QFIs") and sub-accounts of the FIIs. Previously portfolio investment was governed under different laws i.e. the SEBI (Foreign Institutional Investors) Regulations, 1995 ("FII Regulations") for FIIs and their sub-accounts and SEBI circulars dated August 09, 2011 and January 13, 2012 governing QFIs, which are now repealed under the SEBI (Foreign Portfolio Investors) Regulations, 2014 ("FPI Regulations") that govern FPIs and are effective from 7 January 2014.

The FPI Regulations are a step in the right direction towards rationalizing and simplifying the portfolio investments in India for foreign investors, with a view to encourage foreign investment in the Indian securities markets.

SEBI (FOREIGN PORTFOLIO INVESTORS) REGULATIONS, 2014

The activities of the Foreign Portfolio Investor in the Indian capital market are regulated by SEBI (Foreign Portfolio Investors) Regulations, 2014.

DEFINITIONS

"Foreign Portfolio Investor" means a person who satisfies the eligibility criteria and has been registered under FPI Regulations, which shall be deemed to be an intermediary. However, any foreign institutional investor or qualified foreign investor who holds a valid certificate of registration shall be deemed to be a foreign portfolio investor till the expiry of the block of three years for which fees have been paid as per the SEBI (Foreign Institutional Investors) Regulations, 1995.

"Qualified Depository Participant" means a depository participant approved by SEBI to act as qualified depository participant.

"Qualified Foreign Investor" means a person who has opened a dematerialized account with a qualified depository participant as a qualified foreign investor;

"Designated Depository Participant" means a person who has been approved by SEBI under FPI Regulations, 2014.

REGISTRATION OF FOREIGN PORTFOLIO INVESTORS

Any person shall not buy, sell or otherwise deal in securities as a foreign portfolio investor unless it has obtained a certificate granted by the designated depository participant on behalf of SEBI. Further that a qualified foreign investor may continue to buy, sell or otherwise deal in securities subject to the provisions of these regulations, for a period of one year from the date of commencement of these regulations, or until he obtains a certificate of registration as foreign portfolio investor, whichever is earlier.

An application for the grant of certificate as foreign portfolio investor shall be made to the designated depository participant in such form and such fees as prescribed in the regulations.

Can the existing Foreign Institutional Investors (FIIs)/Sub Accounts (SA) continue to buy, sell or deal in securities till the expiry of their current registration without payment of conversion fees during the validity of their registration?

Yes, The existing FIIs/SAs may continue to buy, sell or deal in securities till the expiry of their current registration. Such FII/SAs shall be required to pay conversion fees on or before the expiry of their current registration. At the time of conversion, the FII must return the certificate of registration in original to the DDP

ELIGIBILITY CRITERIA

An applicant desirous of foreign portfolio investor registration should, *inter alia*, satisfy the following conditions:

- It should not be resident in India or a Non-Resident Indian.
- It should be a resident of a country:-
 - whose securities market regulator is a signatory to IOSCO's Multilateral MOU or a signatory to a bilateral MOU with SEBI;
 - whose central bank is a member of the Bank for International Settlements;
 - against whom the Financial Action Task Force (FATF) has not issued any warnings
- It should legally be permitted to invest in securities outside the country of its incorporation or establishment or place of business.
- It should be authorised by its Memorandum of Association and Articles of Association or equivalent document(s) or the agreement to invest on its own behalf or on behalf of its clients.
- It must be a fit and proper person as prescribed.
- the applicant has sufficient experience, good track record, is professionally competent, financially sound and has a generally good reputation of fairness and integrity;
- the grant of certificate to the applicant is in the interest of the development of the securities market;

Whether the existing FIIs and SAs that do not meet the eligibility requirements as stipulated under these regulations, can continue to deal in Indian securities?

Yes. All existing FIIs and SAs are deemed FPIs. They can continue to deal in Indian securities till the validity period of FII/SA registration for which fee has been paid. After the validity period, they can continue to deal as FPIs subject to payment conversion and registration fees.

CATEGORIES OF FPI

An applicant shall seek registration as a foreign portfolio investor in one of the categories mentioned hereunder or any other category as may be specified by SEBI from time to time:

Categories of FPI

Category I FPI includes :

- Government and Government-related investors such as central banks, Governmental agencies, sovereign wealth funds and
- international or multilateral organisations or agencies.

Category II FPIs includes :

- appropriately regulated broad based funds such as mutual funds, investment trusts, insurance/reinsurance companies;
- appropriately regulated persons such as banks, AMCs, investment managers/advisors, portfolio managers;
- broad based funds that are not appropriately regulated but whose investment manager is appropriately regulated.
- university funds and pension funds; and
- university-related endowments already registered with SEBI as FIIs or sub accounts.

Category III FPIs include :

- all others not eligible under Category I and II FPIs such as endowments, charitable societies, charitable trusts, foundations, corporate bodies, trusts, individuals and family offices.

However, the investment manager of such broad based fund should be registered as a Category II FPI and should undertake that it shall be responsible and liable for all acts of commission and omission of all its underlying broad based funds and other deeds and things done by such broad based funds under these regulations.

Explanation 1.- An applicant seeking registration as a foreign portfolio investor shall be considered to be “appropriately regulated” if it is regulated or supervised by the securities market regulator or the banking regulator of the concerned foreign jurisdiction, in the same capacity in which it proposes to make investments in India.

Explanation 2-

(A) “Broad based fund” shall mean a fund, established or incorporated outside India, which has at least twenty investors, with no investor holding more than 49% of the shares or units of the fund. However, if the broad based fund has an institutional investor who holds more than 49% of the shares or units in the fund, then such institutional investor must itself be a broad based fund.

(B) For ascertaining the number of investors in a fund, direct investors as well as underlying investors shall be considered.

(C) Only investors of entities which have been set up for the sole purpose of pooling funds and making investments, shall be considered for the purpose of determining underlying investors.

Whether entities which are not regulated are eligible to be registered as FPIs?

Entities which are not appropriately regulated can register as Category III FPIs.

FURNISHING OF INFORMATION, CLARIFICATION AND PERSONAL REPRESENTATION

SEBI or the designated depository participant may require the applicant to furnish such further information or

clarification as it consider necessary, for the purpose of processing of the application. SEBI or the designated depository participant if so desires, may ask the applicant or its authorised representative to appear before SEBI for personal representation in connection with the grant of a certificate.

GRANT OF CERTIFICATE

The designated depository participant grants a certificate after getting satisfied that the applicant is eligible for the grant of a certificate of registration. The grant of certificate of registration should be subject to the payment of the specified registration fee in the manner prescribed in the regulations.

If an applicant seeking registration as a foreign portfolio investor has any grievance with respect to its application or if the designated depository participant has any question in respect of interpretation of any provision of this regulation, it may approach SEBI for appropriate instructions.

An application for grant of certificate of registration, which is not complete in all respects or is false or misleading in any material particular shall be deemed to be deficient and liable to be rejected by the designated depository participant.

However, before rejecting any such application, the applicant shall be given a reasonable opportunity to remove the deficiency, within the time as specified by the designated depository participant.

PROCEDURE WHERE CERTIFICATE IS NOT GRANTED

The designated depository participant may reject the application if after considering an application is of the opinion that a certificate should not be granted, after giving the applicant a reasonable opportunity of being heard. The decision of the designated depository participant not to grant the certificate should be communicated by the designated depository participant to the applicant stating the grounds on which the application has been rejected. Any applicant aggrieved by the decision of the designated depository participant may apply to SEBI, within a period of thirty days from the date of receipt of communication. SEBI as soon as possible re-consideration the application and after giving a reasonable opportunity of being heard, convey its decision in writing to the applicant.

SUSPENSION, CANCELLATION OR SURRENDER OF CERTIFICATE

The registration granted by the designated depository participant on behalf of SEBI under these regulations shall be permanent unless suspended or cancelled by SEBI or surrendered by the foreign portfolio investor. Suspension and cancellation of registration granted by SEBI under these regulations shall be dealt with in the manner as provided in Chapter V of the Securities and Exchange Board of India (Intermediaries) Regulations, 2008.

Any foreign portfolio investor desirous of giving up its activity and surrendering the certificate of registration may make a request for such surrender to the designated depository participant who shall accept the surrender of registration after obtaining approval from SEBI to do so. While accepting the surrender of registration, the designated depository participant may impose such conditions as may be specified by SEBI and such person shall comply with such conditions.

APPROVAL OF DESIGNATED DEPOSITORY PARTICIPANT

APPLICATION FOR APPROVAL TO ACT AS DESIGNATED DEPOSITORY PARTICIPANT

Any person shall not act as designated depository participant unless it has obtained the approval of SEBI. However, a custodian of securities which is registered with SEBI as on the date of commencement of these regulations shall be deemed to have been granted approval as designated depository participant subject to the payment of fees as prescribed in regulations.

Further, A qualified depository participant which has been granted approval by SEBI prior to the commencement of these regulations, having opened qualified foreign investor account as on date of notification of these regulations,

shall be deemed to have been granted approval as designated depository participant subject to the payment of fees as prescribed in this regulations.

An application for approval to act as designated depository participant shall be made to SEBI through the depository in which the applicant is a participant and shall be accompanied by the application fee specified and shall be paid in the manner specified in the regulations.

The depository shall forward to SEBI the application, as early as possible, but not later than 30 days from the date of receipt by the depository, along with its recommendations and certifying that the participant complies with the eligibility criteria as provided in these regulations.

ELIGIBILITY CRITERIA OF DESIGNATED DEPOSITORY PARTICIPANT

- The SEBI shall not consider an application for the grant of approval as designated depository participant unless the applicant satisfies the following conditions, namely:
 - (a) the applicant is a participant registered with SEBI.
 - (b) the applicant is a custodian of securities registered with SEBI.
 - (c) the applicant is an Authorized Dealer Category-1 bank authorized by RBI;
 - (d) the applicant has multinational presence either through its branches or through agency relationships with intermediaries regulated in their respective home jurisdictions;
 - (e) the applicant has systems and procedures to comply with the requirements of Financial Action Task Force Standards, Prevention of Money Laundering Act, 2002, Rules prescribed thereunder and the circulars issued from time to time by SEBI.
 - (f) the applicant is a fit and proper person based on the criteria specified in Schedule II of the SEBI (Intermediaries) Regulations, 2008; and
 - (g) any other criteria specified by SEBI from time to time.
 - SEBI may consider an application from a global bank, regulated in its home jurisdiction, for grant of approval to act as designated depository participant, if it is satisfied that it has sufficient experience in providing custodial services and the grant of such approval is in the interest of the development of the securities market.
- However, such global bank shall be registered with SEBI as a participant, custodian of securities, and shall have tie up with Authorized Dealer Category-1 bank.
- After considering an application, SEBI may grant approval to the applicant, if it is satisfied that the applicant is eligible and fulfills the requirements including payment of fees.
 - SEBI shall dispose of the application for grant of approval as soon as possible but not later than one month after receipt of application by SEBI or, after the information furnished, whichever is later.
 - An application for grant of approval to act as designated depository participant which is not complete in all respects or is false or misleading in any material particular, shall be deemed to be deficient and shall be liable to be rejected by SEBI after giving a reasonable opportunity to remove the deficiency, within the time as specified by SEBI.

PROCEDURE WHERE APPROVAL IS NOT GRANTED

SEBI may reject the application if the applicant does not satisfied the requirements specified above after giving a reasonable opportunity of being heard and the decision of rejection shall be communicated by SEBI to the applicant in writing stating therein the grounds on which the application has been rejected.

The applicant, who is aggrieved by the decision of SEBI may, within a period of thirty days from the date of

receipt of communication may apply to SEBI for reconsideration of its decision. SEBI shall reconsideration the application after giving a reasonable opportunity of being heard, convey its decision in writing to the applicant.

VALIDITY OF APPROVAL

The approval granted by SEBI shall be permanent unless suspended or withdrawn by SEBI or surrendered by the designated depository participant.

SUSPENSION OR WITHDRAWAL OR SURRENDER OF APPROVAL

Where any designated depository participant who has been granted approval-

- fails to comply with any conditions subject to which an approval has been granted to him;
- contravenes any of the provisions of the securities laws or directions, instructions or circulars issued thereunder;

SEBI may, by order suspend or withdraw such approval after providing a reasonable opportunity of being heard to the designated depository participant. Any designated depository participant, who has been granted approval desirous of giving up its activity and surrendering the approval granted, may make a request for such surrender to SEBI.

SEBI may impose such conditions as it deems fit for protection of investors or the clients of designated depository participants or the securities market and such person shall comply with such conditions.

INVESTMENT CONDITIONS AND RESTRICTIONS

INVESTMENT RESTRICTIONS

- A foreign portfolio investor shall invest only in the following securities, namely-
 - Shares, debentures and warrants of companies, listed or to be listed on a recognized stock exchange in India through primary and secondary markets;
 - Units of schemes floated by domestic mutual funds, whether listed on a recognized stock exchange or not;
 - Units of schemes floated by a collective investment scheme;
 - Derivatives traded on a recognized stock exchange;
 - Treasury bills and dated government securities;
 - Commercial papers issued by an Indian company;
 - Rupee denominated credit enhanced bonds;
 - Security receipts issued by asset reconstruction companies;
 - Perpetual debt instruments and debt capital instruments, as specified by the Reserve Bank of India from time to time;
 - Listed and unlisted non-convertible debentures/bonds issued by an Indian company in the infrastructure sector, where 'infrastructure' is defined in terms of the extant External Commercial Borrowings (ECB) guidelines;
 - Non-convertible debentures or bonds issued by Non-Banking Financial Companies categorized as 'Infrastructure Finance Companies'(IFCs) by the Reserve Bank of India;
 - Rupee denominated bonds or units issued by infrastructure debt funds;
 - Indian depository receipts;
 - Unlisted non-convertible debentures/bonds issued by an Indian company subject to the guidelines issued by the Ministry of Corporate Affairs, Government of India from time to time;

- Securitized debt instruments, including, –
 - (i) any certificate or instrument issued by a special purpose vehicle set up for securitization of asset/s with banks, financial institutions or non-banking financial institutions as originators; and
 - (ii) any certificate or instrument issued and listed in terms of the SEBI (Public Offer and Listing of Securitised Debt Instruments) Regulations, 2008;
- Such other instruments specified by SEBI from time to time.
- Where a foreign institutional investor (FII) or a sub account, prior to commencement of these regulations, holds equity shares in a company whose shares are not listed on any recognized stock exchange, and continues to hold such shares after initial public offering and listing thereof, such shares shall be subject to lock-in for the same period, if any, as is applicable to shares held by a foreign direct investor placed in similar position, under the policy of the Government of India relating to foreign direct investment for the time being in force.
- In respect of investments in the secondary market, the following additional conditions shall apply:
 - a) A foreign portfolio investor shall transact in the securities in India only on the basis of taking and giving delivery of securities purchased or sold;
 - b) Clause (a) shall not apply to, in case of :
 - Any transactions in derivatives on a recognized stock exchange;
 - Short selling transactions in accordance with the framework specified by SEBI;
 - Any transaction in securities pursuant to an agreement entered into with the merchant banker in the process of market making or subscribing to unsubscribed portion of the issue in accordance with SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009;
 - Any other transaction specified by SEBI.
 - c) No transaction on the stock exchange shall be carried forward;
 - d) The transaction of business in securities by a foreign portfolio investor shall be only through stock brokers registered by SEBI.
 - e) Clause (d) shall not apply to, in case of :
 - transactions in Government securities and such other securities falling under the purview of the RBI.
 - sale of securities in response to a letter of offer sent by an acquirer in accordance with the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011;
 - sale of securities in response to an offer made by any promoter or acquirer in accordance with SEBI (Delisting of Equity shares) Regulations, 2009;
 - sale of securities, in accordance with SEBI (Buy-back of securities) Regulations, 1998;
 - divestment of securities in response to an offer by Indian Companies in accordance with Operative Guidelines for Disinvestment of Shares by Indian Companies in the overseas market through issue of ADR or GDR as notified by the Government of India and directions issued by RBI from time to time;
 - any bid for, or acquisition of, securities in response to an offer for disinvestment of shares made by the Central Government or any State Government;
 - any transaction in securities pursuant to an agreement entered into with merchant banker in the

process of market making or subscribing to unsubscribed portion of the issue in accordance with SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009;

- transactions by Category I and II foreign portfolio investors, in corporate bonds, as may be specified by SEBI;
- transactions on the electronic book provider platform of recognized stock exchanges;
- any other transaction specified by SEBI.

f) A foreign portfolio investor shall hold, deliver or cause to be delivered securities only in dematerialized form. However, any shares held in non-dematerialized form, before the commencement of these regulations, can be held in non-dematerialized form, if such shares cannot be dematerialized.

- In respect of investments in the debt securities, the foreign portfolio investors shall also comply with terms, conditions or directions, specified or issued by SEBI or RBI, from time to time, in addition to other conditions specified in these regulations.
- Unless otherwise approved by SEBI, securities shall be registered in the name of the foreign portfolio investor as a beneficial owner for the purposes of the Depositories Act, 1996.
- The purchase of equity shares of each company by a single foreign portfolio investor or an investor group shall be below ten percent of the total issued capital of the company.
- The investment by the foreign portfolio investor shall also be subject to such other conditions and restrictions as may be specified by the Government of India from time to time.
- In cases where the Government of India enters into agreements or treaties with other sovereign Governments and where such agreements or treaties specifically recognize certain entities to be distinct and separate, SEBI may, during the validity of such agreements or treaties, recognize them as such, subject to conditions as may be specified by it.
- A foreign portfolio investor may lend or borrow securities in accordance with the framework specified by SEBI in this regard.

OFFSHORE DERIVATIVE INSTRUMENTS (ODIs)

Offshore Derivative Instrument means any instrument, by whatever name called, which is issued overseas by a foreign portfolio investor against securities held by it that are listed or proposed to be listed on any recognized stock exchange in India or unlisted debt securities or securitised debt instruments, as its underlying.

CONDITIONS FOR ISSUANCE OF OFFSHORE DERIVATIVE INSTRUMENTS (ODIS)

- FPIs can issue, subscribe to or otherwise deal in ODIs, directly or indirectly, only if such ODIs are issued to persons who are regulated by an appropriate foreign regulatory authority, and the ODIs are issued after compliance with 'Know Your Client' (KYC) norms. Such offshore derivative instruments shall not be issued to or transferred to persons who are resident Indians or non-resident Indians and to entities that are beneficially owned by resident Indians or non-resident Indians.
- Unregulated broad based funds which are classified as Category II FPIs by virtue of their investment manager being appropriately regulated shall not deal in ODIs.
- Category III FPIs also cannot deal in ODIs.
- FPIs shall ensure that further issue or transfer of any ODIs issued by or on behalf of it is made only to persons who are regulated by an appropriate foreign regulatory authority.
- Foreign portfolio investors shall fully disclose to SEBI any information concerning the terms of and parties to off-shore derivative instruments such as participatory notes, equity linked notes or any other

such instruments, by whatever names they are called, entered into by it relating to any securities listed or proposed to be listed in any stock exchange in India.

- Outstanding ODIs shall be deemed to have been issued under the corresponding provision of the FPI Regulations.

SEBI has issued Clarification on **Guidelines for issuance of ODIs, with derivative as underlying, by the ODI issuing FPIs**. In this direction, the ODI issuing FPIs shall not be allowed to issue ODIs with derivative as underlying. Derivative positions that are taken by the ODI-issuing FPI for hedging the equity shares held by it on a one to one basis are being exempted.

In case, where underlying derivative position are not for purpose of hedging the equity shares held by it, the ODI issuing FPI has to liquidate such ODIs latest by the date of maturity of the ODI instrument or by December 31, 2020, whichever is earlier. SEBI has advised ODI-issuing FPIs to liquidate such ODI instruments prior to the timeline. A certificate has to be issued by the compliance officer of the ODI-issuing FPI for issuance of fresh ODIs with derivatives as underlying.

KNOW YOUR CLIENT (KYC) NORMS FOR ODI SUBSCRIBERS

ODI Issuers shall now be required to identify and verify the beneficial owners (BO) in the subscriber entities, who hold in excess of the 25 % in case of a company and 15 % in case of partnership firms/ trusts/ unincorporated bodies under Rule 9 of the Prevention of Money-laundering (Maintenance of Records) Rules, 2005.

ODI issuers shall also be required to identify and verify the person(s) who control the operations, when no beneficial owner is identified based on the aforesaid materiality threshold. SEBI clarified the following in respect of ODIs:

- The KYC documentation shall be obtained by ODI Issuers from each of such ODI subscribers in respect of beneficial owner who holds above the threshold limits in such ODI subscriber.
- The materiality threshold referred above, to identify the beneficial owner should be first applied at the ODI subscriber level and look through principle shall be applied to identify the beneficial owner of the material shareholder/ owner entity.
- Only beneficial owner with holdings equal & above the materiality thresholds in the subscriber need to be identified through the aforesaid look through principle. In such cases, identity and address proof should be obtained.
- Where no material shareholder/owner entity is identified in the ODI subscriber using the materiality threshold, the identity and address proof of the relevant natural person who holds the position of senior managing official of the material shareholder/owner entity should be obtained.
- Any transfer of ODIs issued by or on its behalf is carried out subject to the following conditions :
 - a) such ODIs are transferred only to persons in accordance with this regulation and
 - b) Prior consent of the FPI must be obtained for such transfer.

The ODI issuers shall be required to maintain KYC documents as prescribed above at all times and should be made available to SEBI on demand.

OBLIGATIONS AND RESPONSIBILITIES OF FOREIGN PORTFOLIO INVESTORS (FPIs)

1. The foreign portfolio investor shall –

- comply with the provisions of these regulations, circulars and any other terms and conditions specified by SEBI from time to time;
- forthwith inform SEBI and designated depository participant in writing, if any information or particulars previously submitted to SEBI or designated depository participant are found to be false or misleading, in any material respect;

- forthwith inform SEBI and designated depository participant in writing, if there is any material change in the information previously furnished by him to SEBI or designated depository participant;
 - as and when required by SEBI or any other government agency in India, submit any information, record or documents in relation to its activities as a foreign portfolio investor;
 - forthwith inform SEBI and the designated depository participant, in case of any penalty, pending litigations or proceedings, findings of inspections or investigations for which action may have been taken or is in the process of being taken by an overseas regulator against it;
 - obtain a Permanent Account Number from the Income Tax Department;
 - in relation to its activities as foreign portfolio investor, at all times, subject itself to the extant Indian laws, rules, regulations and circulars issued from time to time and provide an express undertaking to this effect to the designated depository participant;
 - provide such declarations and undertakings as required by the designated depository participant; and
 - provide any additional information or documents as may be required by the designated depository participant to ensure compliance with the Prevention of Money Laundering Act, 2002 and rules and regulations prescribed thereunder, Financial Action Task Force standards and circulars issued from time to time by SEBI.
2. In case of jointly held depository accounts, each of the joint holders shall meet the requirements specified for foreign portfolio investor and each shall be deemed to be holding a depository account as a foreign portfolio investor.
3. In case the same set of ultimate beneficial owner(s) invest through multiple entities, such entities shall be treated as part of same investor group and the investment limits of all such entities shall be clubbed at the investment limit as applicable to a single foreign portfolio investor.
4. In case of any direct or indirect change in structure or beneficial ownership of the foreign portfolio investor, it shall bring the same to the notice of its designated depository participant forthwith.

CODE OF CONDUCT

Every foreign portfolio investor is required to abide by the Code of Conduct as per SEBI Regulations:

- A foreign portfolio investor and its key personnel shall observe high standards of integrity, fairness and professionalism in all dealings in the Indian securities market with intermediaries, regulatory and other government authorities.
- A foreign portfolio investor shall, at all times, render high standards of service, exercise due diligence and independent professional judgment.
- A foreign portfolio investor shall ensure and maintain confidentiality in respect of trades done on its own behalf and/or on behalf of its clients.
- A foreign portfolio investor shall ensure the clear segregation of its own money/securities and its client's money/securities and arms length relationship between its business of fund management/investment and its other business.
- A foreign portfolio investor shall maintain an appropriate level of knowledge and competency and abide by the provisions of the Act, regulations made thereunder and the circulars and guidelines, which may be applicable and relevant to the activities carried on by it. Every foreign portfolio investor shall also comply with award of the Ombudsman and decision of SEBI under SEBI (Ombudsman) Regulations, 2003.
- A foreign portfolio investor shall not make any untrue statement or suppress any material fact in any documents, reports or information to be furnished to the designated depository participant and/or SEBI.
- A foreign portfolio investor shall ensure that good corporate policies and corporate governance are observed by it.

- A foreign portfolio investor shall ensure that it does not engage in fraudulent and manipulative transactions in the securities listed in any stock exchange in India.
- A foreign portfolio investor or any of its directors or managers shall not, either through its/his own account or through any associate or family members, relatives or friends indulge in any insider trading.
- A foreign portfolio investor shall not be a party to or instrumental for –
 - creation of false market in securities listed or proposed to be listed in any stock exchange in India;
 - price rigging or manipulation of prices of securities listed or proposed to be listed in any stock exchange in India;
 - passing of price sensitive information to any person or intermediary in the securities market.

APPOINTMENT OF CUSTODIAN OF SECURITIES

A foreign portfolio investor or a global custodian, who is acting on behalf of the foreign portfolio investor, shall enter into an agreement with the designated depository participant engaged by it to act as a custodian of securities, before making any investment under these regulations. In addition to the obligation of custodian of securities under any other regulations.

The custodian of securities shall :



APPOINTMENT OF DESIGNATED BANK

A foreign portfolio investor shall appoint a branch of a bank authorized by the Reserve Bank of India for opening of foreign currency denominated account and special non-resident rupee account before making any investments in India.

OBLIGATIONS AND RESPONSIBILITIES OF DESIGNATED DEPOSITORY PARTICIPANTS (DDPs)

- All designated depository participants (DDPs) who have been granted approval by SEBI shall –
 - Comply with the provisions of these regulations, circulars and any other terms and conditions specified by SEBI from time to time;
 - Forthwith inform SEBI in writing, if any information or particulars previously submitted to SEBI are found to be false or misleading, in any material respect;

- Forthwith inform SEBI in writing, if there is any material change in the information previously furnished by him to SEBI.
- Furnish such information, record or documents to SEBI and RBI, as may be required, in relation to his activities as a DDP.
- Ensure that only registered foreign portfolio investors are allowed to invest in securities market.
- Ensure that foreign portfolio investor does not have opaque structure(s).

Explanation- “Opaque structure” mean any structure such as protected cell company, segregated cell company or equivalent, where the details of the ultimate beneficial owners are not accessible or where the beneficial owners are ring fenced from each other or where the beneficial owners are ring fenced with regard to enforcement.

However, the foreign portfolio investor satisfying the following criteria shall not be treated as having opaque structure:

- The applicant is regulated in its home jurisdiction
- Each fund or sub fund in the applicant satisfies broad based criteria, and
- The applicant gives an undertaking to provide information regarding its beneficial owners as and when Board seeks this information.
 - have adequate systems to ensure that in case of jointly held depository accounts, each of the joint holders meet the requirements specified for foreign portfolio investors and shall perform KYC due diligence for each of the joint holders;
 - in case of any penalty, pending litigations or proceedings, findings of inspections or investigations for which action may have been taken or is in the process of being taken by any regulator against a DDP, the DDP shall bring such information forthwith, to the attention of SEBI, depositories and stock exchanges;
 - be guided by the relevant circular on Anti-Money Laundering or Combating the Financing of Terrorism specified by SEBI from time to time.
- The designated depository participant engaged by an applicant seeking registration as foreign portfolio investor shall:-
 - ascertain at the time of granting registration and whenever applicable, whether the applicant forms part of any investor group;
 - open a dematerialized account for the applicant only after ensuring compliance with all the requirements under Prevention of Money Laundering Act, 2002 and rules and regulations prescribed thereunder, Financial Action Task Force standards and circulars issued by SEBI in this regard, from time to time and shall also ensure that foreign portfolio investors comply with all these requirements on an on going basis;
 - carry out necessary due diligence and obtain appropriate declarations and undertakings from applicant to ensure that no other depository account is held by any of the concerned applicant as a foreign portfolio investor or as a non-resident Indian, before opening a depository account;
 - ensure that equity shares held by foreign portfolio investors are free from all encumbrances;
 - collect and remit fees to SEBI, in the manner as specified in Part A of Second Schedule; and
 - in case of change in structure or constitution or direct or indirect change in beneficial ownership reported by the foreign portfolio investor, re-assess the eligibility of such foreign portfolio investor.

APPOINTMENT OF COMPLIANCE OFFICER

Every foreign portfolio investor and DDPs shall appoint a compliance officer who shall be responsible for monitoring the compliance of the Act, rules and regulations, notifications, guidelines and instructions issued by the designated depository participant (in case of FPIs) or SEBI or the Central Government. The compliance officer shall immediately and independently report to SEBI and the designated depository participant regarding any non-compliance observed by him.

INVESTMENT ADVICE IN PUBLICLY ACCESSIBLE MEDIA

A foreign portfolio investor, or designated depository participant or any of its employees shall not render directly or indirectly any investment advice about any security in the publicly accessible media, whether real-time or non-real-time, unless a disclosure of his interest including long or short position in the said security has been made, while rendering such advice.

In case, an employee of the foreign portfolio investor or designated depository participant is rendering such advice, he shall also disclose the interest of his dependent family members and his employer including their long or short position in the said security, while rendering such advice.

MAINTENANCE OF PROPER BOOKS OF ACCOUNTS, RECORDS AND DOCUMENTS

- Every foreign portfolio investor shall keep or maintain, as the case may be, the following books of accounts, records and documents, namely:-
 - true and fair accounts relating to remittance of initial corpus for buying, selling and realising capital gains of investment made from the corpus;
 - accounts of remittances to India for investments in India and realising capital gains on investments made from such remittances;
 - bank statement of accounts;
 - contract notes relating to purchase and sale of securities; and
 - communication from and to the designated depository participants, stock brokers and depository participants regarding investments in securities.
- Every designated depository participant shall keep or maintain, as the case may be, the relevant true and fair records, books of accounts, and documents including the records relating to registration of foreign portfolio investors.
- The foreign portfolio investor shall intimate to its designated depository participants and DDP shall intimate to SEBI in writing, the location where such books, records and documents will be kept or maintained.
- Every foreign portfolio investor and DDPs shall preserve the books of accounts, records and documents for a minimum period of five years.

PROCEDURE FOR INSPECTION AND INVESTIGATION

SEBI can appoint one or more persons as inspecting authority to undertake inspection and investigation of the books of account, records and documents relating to a designated depository participant for any of the following purposes, namely,-

- To ensure that the books of account, records including telephone records and electronic records and documents are being maintained by DDPs.
- To ascertain whether any circumstances exist which would render the DDPs unfit or ineligible;

- To inquire into the complaints received from investors, clients, other market participants or any other person on any matter having a bearing on the activities of the DDPs.
- To ascertain whether the provisions of the securities laws and the directions or circulars issued are complied.
- To ascertain whether the systems, procedures and safeguards which have been established and are being followed by DDPs are adequate; and
- To investigate suo motu into the affairs of DDPs in the interest of the securities market or in the interest of investors.

NOTICE OF INSPECTION OR INVESTIGATION

SEBI shall give ten days written notice to the DDPs before ordering an inspection or investigation. SEBI in the interest of the investors may order in writing, direct that the inspection or investigation of the affairs of the DDPs to be taken up without such notice. During the course of an inspection or investigation, the DDPs against whom the inspection or investigation is being carried out should be bound to discharge all its obligations as provided in this regulation.

OBLIGATIONS OF DESIGNATED DEPOSITORY PARTICIPANTS IN INSPECTION

- It shall be the duty of the designated depository participants whose affairs are being inspected, and of every director, officer and employee thereof :-
 - to produce such books, securities, accounts, records and other documents in its custody or control to the inspecting officer and
 - furnish such statements and information relating to its activities, as the inspecting officer may require, within such reasonable period as the inspecting officer may specify.
- The designated depository participants shall allow :
 - the inspecting officer to have reasonable access to the premises occupied by such designated depository participant or by any other person on its behalf and
 - also extend reasonable facility for examining any books, records, documents and computer data in the possession of the designated depository participants or such other person and
 - provide copies of documents or other materials which in the opinion of the inspecting officer are relevant for the purposes of the inspection.
- The inspecting officer, in the course of inspection, shall be entitled to examine or to record the statements of any director, officer or employee of the designated depository participants.
- It shall be the duty of every director, officer or employee of the designated depository participants to give to the inspecting officer all assistance in connection with the inspection, which the inspecting officer may reasonably require.

SUBMISSION OF REPORT TO SEBI

The inspecting officer shall, as soon as possible, on completion of the inspection or investigation as the case may be, submit a report to SEBI and if directed to do so by SEBI, he may submit interim report(s). SEBI shall after consideration of inspection report take such action as SEBI may deem fit and appropriate including action under Chapter V of the SEBI (Intermediaries) Regulations, 2008.

APPOINTMENT OF AUDITOR

SEBI have the power to appoint an auditor to inspect or investigate, as the case may be, into the books of account, records, documents, infrastructures, systems and procedures or affairs of the applicant or the designated depository participants, as the case may be.

However, the auditors so appointed shall have the same powers as vested in the inspecting officer as prescribed in the regulation and the applicant or designated depository participants and its directors, officers and employees shall be under the same obligations, towards the auditor so appointed, as are mentioned in regulation.

SEBI shall be entitled to recover from the designated depository participants or applicant, as the case may be, such expenses including fees paid to the auditors as may be incurred by it for the purposes of inspecting or investigating the books of account, records, documents, infrastructures, systems and procedures or affairs of the designated depository participants or applicant, as the case may be.

ACTION IN CASE OF DEFAULT

A foreign portfolio investor, designated depository participant, depository or any other person who contravenes any of the provisions of these regulations shall be liable for action under SEBI (Intermediaries) Regulations, 2008 and/or the relevant provisions of the Act or the Depositories Act, 1996.

LESSON ROUND UP

- SEBI notified the foreign portfolio Investors Regulations to encourage and simplify foreign portfolio investments.
- This Regulation has replaced the existing SEBI (Foreign Institutional Investor) Regulations, 1995 (FII Regulations) and the Qualified Foreign Investors (QFI) framework and are effective from 7 January 2014.
- SEBI has classified FPI into three broad categories i.e. Category I, Category II, Category III.
- All FPIs are required to be mandatorily registered under any one of the above mentioned categories.
- The records maintained by FPI/DDP is required to be maintained for a period of five years.
- Custodian of securities means any person who carries on or proposes to carry on the business of providing custodial services.
- FPIs and DDPs are required to appoint a compliance officer who shall be responsible for monitoring the compliance of the Act, rules and regulations, notifications, guidelines, instructions etc. issued by SEBI or Central Government Compliance officer is required to immediately and independently report to SEBI, any non-compliance observed by him.

GLOSSARY

IOSCO	International Organization of Securities Commissions
Broad based	Means a fund, established or incorporated outside India, which has fund at least twenty investors, with no investor holding more than 49% of the shares or units of the fund.
Bilateral MOU	It's a bilateral MOU between SEBI and the Overseas regulator that <i>inter alia</i> , provides for information sharing arrangements under sub-section (2) (ib) of section 11 of this Act.

SELF TEST QUESTIONS

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation.)

1. Explain general obligations and responsibilities of FPIs as per SEBI (Foreign Portfolio Investors) Regulation, 2014.
2. Discuss the procedure relating to inspection and investigation of the Foreign Portfolio Investors.
3. Explain major provisions of SEBI (Foreign Portfolio Investors) Regulation, 2014.
4. Discuss the type of securities where FPIs can invest its money and restrictions imposed as per the SEBI (Foreign Portfolio Investors) Regulation, 2014.
5. What are the eligibility criteria for approval of DDPs?
6. Explain the obligations and responsibilities of FPIs as per SEBI (Foreign Portfolio Investors) Regulation, 2014.

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Lesson 13

Non-Convertible Redeemable Preference Shares

LESSON OUTLINE

- Introduction
- SEBI (Issue and Listing of Non-Convertible Redeemable Preference Shares) Regulations, 2013
- Definitions
- Issue of Non-Convertible Redeemable Preference Shares
- Conditions For Private Placement
- Listing and Trading of Non-Convertible Redeemable Preference Shares
- Obligations of the Issuer and Lead Merchant Banker etc.
- Issuance and Listing of Non-Equity Regulatory Capital Instruments by Banks
- Inspection by SEBI
- Powers of SEBI
- LESSON ROUND UP
- GLOSSARY
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

With an aim to bring more transparency in raising funds through non-convertible preference shares, the Capital Market Regulator, SEBI has notified a new set of Regulations to govern issuance and listing of Non-Convertible Redeemable Preference Shares (NCRPS), to be called SEBI (Issue and Listing of Non-Convertible Redeemable Preference Shares) Regulations, 2013. Non-convertible preference shares is an another instrument for raising fund from public to Indian companies.

This Lesson is design to enable the student to understand Issue and listing of Non-convertible Redeemable Preference Shares, Obligations of the issuer and lead merchant banker, Issuance & Listing of Non-Equity Regulatory Capital Instruments by banks and Inspection and Power of SEBI.

INTRODUCTION

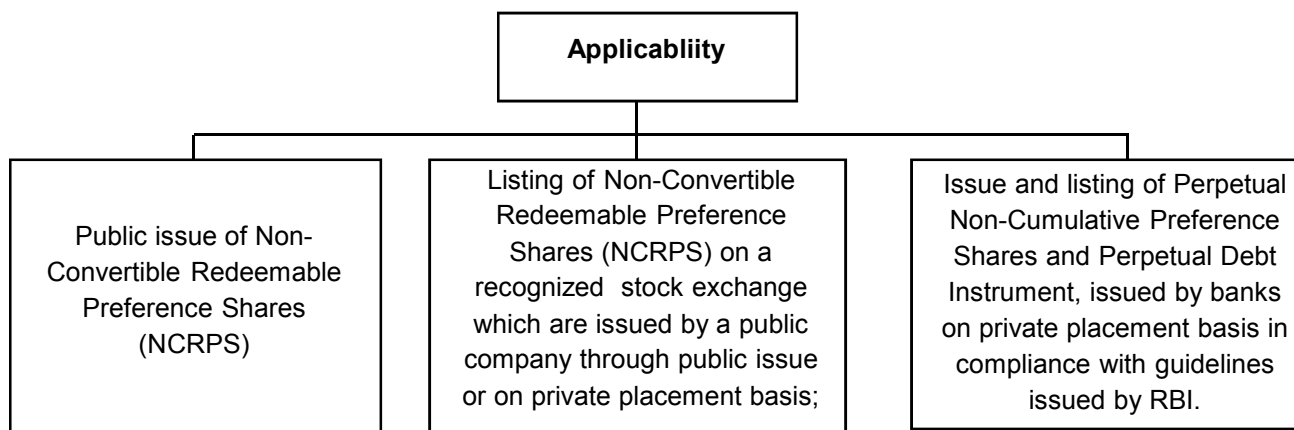
SEBI has notified the SEBI (Issue and Listing of Non-Convertible Redeemable Preference Shares) Regulations, 2013 to govern big issues of non convertible redeemable preference shares. Preference shares, in general, are fairly common among the foreign investors, venture capital investors and so on as such instruments give preference in dividend and at the same time have other features of ordinary debentures.

There are SEBI (Issue and Listing of Debt Securities) Regulations, 2008 which govern non-convertible debt securities and issue of equity and convertible securities by a listed company are governed by SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009. However, there were no such regulation which governed the issue and listing of non-convertible redeemable preference shares. A huge fund raising through non-convertible redeemable preference shares, then SEBI had decided to govern the issue of such shares and in this direction notified the SEBI (Issue and Listing of Non-Convertible Redeemable Preference Shares) Regulations, 2013.

SEBI (ISSUE AND LISTING OF NON-CONVERTIBLE REDEEMABLE PREFERENCE SHARES) REGULATIONS, 2013

SEBI issued (Issue and Listing of Non-Convertible Redeemable Preference Shares) Regulations, 2013 pertaining to Issue and Listing of Non-Convertible Redeemable Preference Shares which are not convertible, either in whole or part into equity instruments. They provide for a rationalized disclosure requirements and a reduction of certain onerous obligations erstwhile attached to an issue of Non-Convertible Redeemable Preference securities.

These regulations are applicable to -



DEFINITIONS

"Non-Convertible Redeemable Preference Share" means a preference share which is redeemable in accordance with the provisions of the Companies Act, 2013 and does not include a preference share which is convertible into or exchangeable with equity shares of the issuer at a later date, with or without the option of the holder.

"Perpetual Non-Cumulative Preference Share" means a perpetual Non-Cumulative Preference Share issued by a bank in accordance with the guidelines framed by the Reserve Bank of India.

"Innovative Perpetual Debt Instrument" means an innovative perpetual debt instrument issued by a bank in accordance with the guidelines framed by the Reserve Bank of India;

"Wilful Defaulter" means any person who is categorized as a wilful defaulter by any bank or financial institution or consortium thereof, in accordance with the guidelines on wilful defaulters issued by the RBI and includes any person whose director, promoter or principal officer is categorized as such.

ISSUE OF NON-CONVERTIBLE REDEEMABLE PREFERENCE SHARES**CONDITIONS**

A company cannot make any public issue of NCRPS unless the following conditions are fulfilled –

1. The company shall not make any public issue of NCRPS if as on the date of filing of draft offer document or final offer document as provided :-
 - the company or the person in control of the company or its promoter or its director is restrained or prohibited or debarred by SEBI from accessing the securities market or dealing in securities; or
 - the company or any of its promoters or directors is a wilful defaulter or it is in default of payment of interest or repayment of principal amount in respect of NCRPS issued by it to the public, if any, for a period of more than 6 months.
2. It has made an application to one or more recognized stock exchanges for listing of such securities therein. If the application is made to more than one recognized stock exchanges, the issuer must choose one of them which has nationwide trading terminals as the designated stock exchange.
3. It has obtained in-principle approval for listing of its non-convertible redeemable preference shares.
4. Credit rating including the unaccepted ratings obtained from more than one credit rating agencies, registered with SEBI shall be disclosed in the offer document.
5. The minimum tenure of the NCRPS shares shall not be less than three years.
6. The issue has been assigned a rating of not less than “AA-” or equivalent by a credit rating agency registered with SEBI.
7. The Company shall create a capital redemption reserve in accordance with the provisions of the Companies Act, 2013.
8. The issuer shall not issue NCRPS for providing loan to or acquisition of shares of any person who is part of the same group or who is under the same management, other than to subsidiaries of the issuer.

APPOINTMENT OF INTERMEDIARIES

1. It shall enter into an arrangement with a depository registered with SEBI for dematerialization of the NCRPS in accordance with the Depositories Act, 1996 and regulations made there under.
2. In case of public issue of NCRPS, the company shall appoint one or more merchant bankers registered with SEBI at least one of whom shall be a lead merchant banker.

DISCLOSURES OF MATERIAL INFORMATION

1. The offer document must contain all material disclosures which are necessary for the subscribers of the NCRPS to take an informed investment decision. The offer document contains the following :
 - (a) the disclosures specified in Section 26 of the Companies Act, 2013;
 - (b) disclosure specified in Schedule I of these regulations;
 - (c) additional disclosures as may be specified by SEBI
2. The amount of minimum subscription which the issuer seeks to raise and underwriting arrangements shall be disclosed in the offer document.

FILING

The company shall file draft offer document with the designated stock exchange through the lead merchant

banker and also forwarded a copy of draft and final offer document to SEBI for its records, along with fees as specified in regulation.

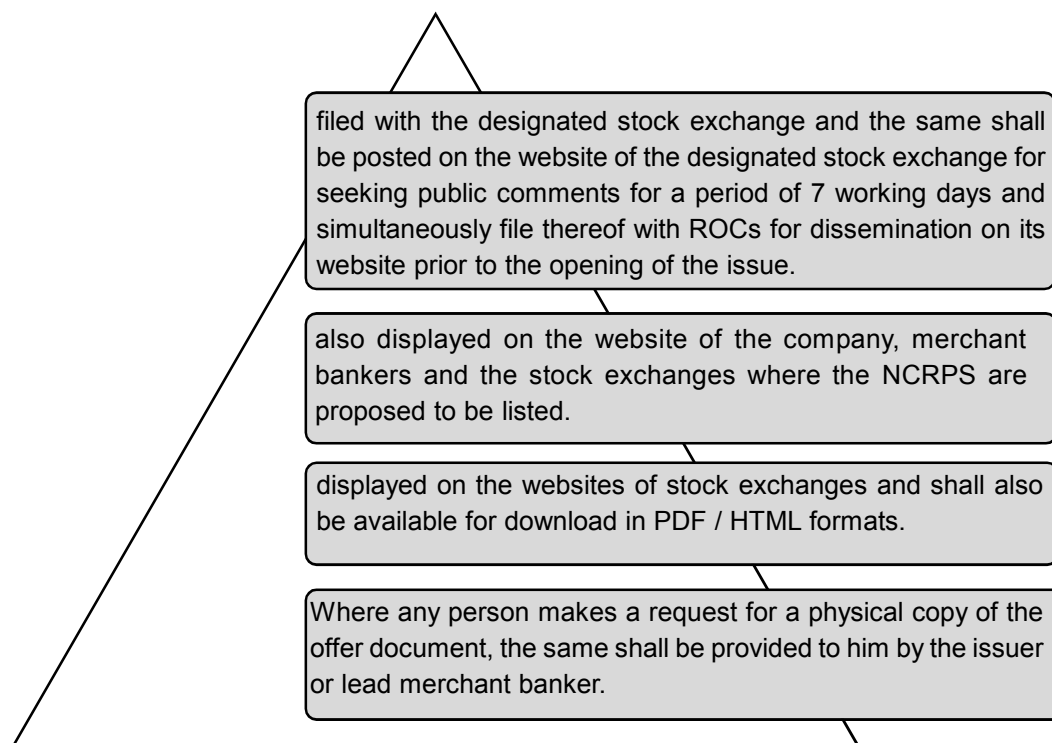
RESPONSIBILITIES OF MERCHANT BANKER

The lead merchant banker must ensure that –

- The draft offer document clearly specifies the names and contact particulars of the compliance officer of the lead merchant banker and the issuer including the postal and email address, telephone and fax numbers.
- All comments received on the draft offer document are suitably addressed and shall also furnish to SEBI a due diligence certificate as per these regulations prior to the filing of the offer document with the Registrar of Companies.

MODE OF DISCLOSURE

The draft offer document shall be:-



ADVERTISEMENTS

- The company should make an advertisement in one English national daily newspaper and one Hindi national daily newspaper with wide circulation on or before the issue opening date and such advertisement, amongst other things must contain the disclosures specified in these regulations.
- A company should not issue an advertisement –
 - which is misleading in material particular or which contains any information in a distorted manner or which is manipulative or deceptive or extraneous matters.

- which contain a statement, promise or forecast which is untrue or misleading and the advertisement shall be truthful, fair and clear.
- during the subscription period any reference to the issue of NCRPS or be used for solicitation.
- The advertisement shall urge the investors to invest only on the basis of information contained in the offer document.

ABRIDGED PROSPECTUS AND APPLICATION FORMS

The issuer and lead merchant banker shall ensure that:

(a) Every application form issued by the issuer is accompanied by a copy of the abridged prospectus;

(b) The abridged prospectus shall not contain matters which are extraneous to the contents of the prospectus;

(c) Adequate space shall be provided in the application form to enable the investors to fill in various details like name, address, etc.

The issuer may provide the facility for subscription of application in electronic mode.

ON-LINE ISSUANCES

A company proposing to issue of NCRPS to the public through the on-line system of the designated stock exchange shall comply with the relevant applicable requirements as may be specified by SEBI.

ISSUE PRICE

A Company may determine the price of NCRPS in consultation with the lead merchant banker and the issue may be at fixed price or the price may be determined through book building process in accordance with the procedure as may be specified by SEBI.

MINIMUM SUBSCRIPTION

The company may decide the amount of minimum subscription which it seeks to raise by public issue of NCRPS in accordance with the provisions of Companies Act, 2013 and disclose the same in the offer document.

In the event of non-receipt of minimum subscription, all application moneys received in the public issue shall be refunded forthwith to the applicants. In the event the application monies are refunded beyond 8 days from the last day of the offer, then such amounts shall be refunded together with interest at such rate as may be set out in the offer document which shall not be less than 15% per annum.

OPTIONAL UNDERWRITING

A public issue of NCRPS may be underwritten by an underwriter registered with SEBI and in such a case adequate disclosures regarding underwriting arrangements shall be made in the offer document.

PROHIBITION OF MIS-STATEMENTS IN THE OFFER DOCUMENT

- The offer document shall not omit disclosure of any material fact which may make the statements made therein, in light of the circumstances under which they are made, misleading.
- The offer document or abridged prospectus or any advertisement issued by an issuer in connection with a public issue of NCRPS shall not contain any false or misleading statement.

MANDATORY LISTING

- A company desirous of making an offer of NCRPS to public shall make an application for listing to one or more recognized stock exchanges in terms of section 40 of the Companies Act, 2013.
- It must comply with conditions of listing of such NCRPS as specified in the Listing Agreement with the stock exchange where such non-convertible redeemable preference shares are sought to be listed.
- Where the company has disclosed the intention to seek listing of NCRPS issued on private placement basis, it shall forward the listing application along with the disclosures specified in Schedule I to these regulation to the recognized stock exchange within fifteen days from the date of allotment of such NCRPS.

LISTING AGREEMENT

Every issuer desirous of listing its non-convertible redeemable preference shares, or perpetual non-cumulative preference shares or innovative perpetual debt instruments on a recognized stock exchange, shall execute an agreement with such stock exchange.

Every issuer who has previously entered into agreements with a recognized stock exchange to list non-convertible redeemable preference shares, or perpetual non-cumulative preference shares or innovative perpetual debt instruments shall execute a fresh listing agreement with such stock exchange within 6 months of the date of notification of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015.

SECURITY DEPOSIT

The issuer shall deposit, before the opening of subscription list, and keep deposited with the stock exchange(s) an amount calculated at the rate of 1% of the amount of securities offered for subscription to the public. The amount stipulated in above shall be deposit and refundable or forfeitable in the manner specified by SEBI.

CONDITIONS FOR PRIVATE PLACEMENT

1. An issuer may list its NCRPS issued on private placement basis on a recognized stock exchange subject to the following conditions:
 - In compliance with the provisions of the Companies Act, 2013, rules prescribed thereunder and other applicable laws;
 - Credit rating has been obtained from at least one credit rating agency registered with SEBI.
 - Should be in dematerialized form;
 - The disclosures as provided in regulation have been made;
 - The minimum application size for each investor is not less than 2 lakh rupees; and
 - Where the application is made to more than one recognized stock exchange, the issuer shall choose one of them as the designated stock exchange.

2. The issuer shall comply with conditions of listing of such NCRPS as specified in the Listing Agreement with the stock exchange where such NCRPS are sought to be listed.
3. The issuer making a private placement of NCRPS and seeking listing thereof on a recognized stock exchange shall make disclosures as specified in Schedule I of these regulations accompanied by the latest Annual Report of the issuer.
4. The disclosures as provided above shall be made on the websites of stock exchanges where such securities are proposed to be listed and shall be available for download in PDF / HTML formats.

RELAXATION OF STRICT ENFORCEMENT OF RULE 19 OF SECURITIES CONTRACTS (REGULATION) RULES, 1957

In exercise of the powers conferred by sub-rule (7) of rule 19 of the Securities Contracts (Regulations) Rules, 1957, SEBI hereby relaxes the strict enforcement of sub-rules (1) and (3) of rule 19 of the said rules in relation to listing of NCRPS issued by way of a public issue or a private placement.

LISTING AND TRADING OF NON-CONVERTIBLE REDEEMABLE PREFERENCE SHARES

CONTINUOUS LISTING

All the issuers making public issues of non-convertible redeemable preference shares or seeking listing of non-convertible redeemable preference shares issued on private placement basis shall comply with the conditions of listing specified in the respective listing agreement for NCRPS.

The issuer and stock exchanges shall disseminate all information and reports on NCRPS including compliance reports filed by the issuers regarding the NCRPS to the investors and the general public by placing them on their websites.

TRADING

1. The NCRPS issued to the public or on a private placement basis, which are listed in recognized stock exchanges, shall be traded and such trades shall be cleared and settled in recognized stock exchanges it should satisfy the conditions specified by SEBI.
2. In case of trades of NCRPS which have been made over the counter, such trades shall be reported on a recognized stock exchange having a nation-wide trading terminal or such other platform as may be specified by SEBI.
3. SEBI may specify conditions for reporting of trades on the recognized stock exchange or other platform.

OBLIGATIONS OF THE ISSUER, LEAD MERCHANT BANKER, ETC.

1. The issuer shall disclose all the material facts in the offer documents issued or distributed to the public and shall ensure that all the disclosures made in the offer document are true, fair and adequate and there is no mis-leading or untrue statements or mis-statement in the offer document.
2. The Merchant Banker shall verify and confirm that the disclosures made in the offer documents are true, fair and adequate and ensure that the issuer is in compliance with these regulations as well as all transaction specific disclosures required as per Companies Act, 2013.
3. The issuer shall treat the applicants in a public issue of NCRPS in a fair and equitable manner as per the procedures as may be specified by SEBI.
4. The intermediaries shall be responsible for the due diligence in respect of assignments undertaken by them in respect of issue, offer and distribution of securities to the public.

5. No person shall employ any device, scheme or artifice to defraud in connection with issue or subscription or distribution of NCRPS which are listed or proposed to be listed on a recognized stock exchange.

ISSUANCE AND LISTING OF NON-EQUITY REGULATORY CAPITAL INSTRUMENTS BY BANKS

The provisions of these regulations shall also, apply to the issuance and listing of Perpetual Non-Cumulative Preference Shares and Innovative Perpetual Debt Instruments by banks. Only a bank may issue such instruments subject to the prior approval and in compliance with the guidelines issued by RBI.

If a bank is incorporated as a company under Companies Act, 2013, it shall, in addition, comply with the provisions of Companies Act, 2013 and/or other applicable statutes. The bank shall comply with the terms and conditions as may be specified by SEBI from time to time and shall make adequate disclosures in the offer document regarding the features of these instruments and relevant risk factors and if such instruments are listed, shall comply with the listing requirements.

INSPECTION BY SEBI

Regulation 24 provides that SEBI may, appoint one or more persons to undertake the inspection and investigation of the books of account, records and documents of the issuer or merchant banker or any other intermediary associated with the public issue, disclosure or listing of NCRPS as governed under these regulations.

SEBI may by a general or special order or circular specify any conditions or requirement in respect of issue of NCRPS. Such orders or circulars may provide for all or any of the following matters, namely:

- (a) Electronic issuances and other issue procedures including the procedure for price discovery;
- (b) Conditions governing trading, reporting, clearing and settlement of trade in NCRPS; or
- (c) Listing conditions.

If any special order is proposed to be issued to any particular issuer or intermediary on a specific issue, no such order shall be issued unless an opportunity to represent is given to the person affected by such order.

LESSON ROUND UP

- Non-Convertible Redeemable Preference Share are a preference share other than a preference share which is convertible into or exchangeable with equity shares of the issuer at a later date, with or without the option of the holder.
- Minimum tenure of the NCRPS shall not be less than three years. The company is required to file draft document with stock exchange through merchant banker and the same shall be displayed on the website of the issuer, merchant bankers and the stock exchanges where the NCRPS are proposed to be listed.
- The issuer shall redeem the NCRPS in terms of the offer document.
- The Companies desirous of making an offer of NCRPS to the public shall make an application for listing to one or more recognized stock exchanges and the company shall enter into listing agreement with the stock exchange where such NCRPS are sought to be listed.
- Perpetual Non-Cumulative Preference Shares and Innovative Perpetual Debt Instruments may issue by banks subject to the prior approval and in compliance with the guidelines issued by RBI.

Lesson 14

Real Estate Investment Trusts

LESSON OUTLINE

- Introduction
- SEBI (Real Estate Investment Trust) Regulations, 2014
- Registration of Real Estate Investment Trusts
- Issue and Listing of Units
- Guidelines for Public Issue of Units of REITs
- Investment conditions, related party transactions, Borrowing and valuation of assets
- Rights and Meetings of Unit Holders
- Disclosures
- Liability for action in Case of Default
- LESSON ROUND UP
- GLOSSARY
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

Real Estate Investment Trusts (REITs) are often described as avenue that offer investors the opportunity to invest in a professionally managed portfolio of real estate, through the purchase of a public-traded investment product.

REITs are collective investment schemes that invest in a portfolio of income generating real estate assets such as shopping malls, offices, hotels or serviced apartments, usually established with a view to generating income for unit holders. REITs are structured as trusts and thus the assets of a REIT are held by an independent trustee on behalf of unitholders.

This lesson is design to understand the concept of REIT, Guidelines for public issue of units of REIT, registration of REITs, Issue and listing of units in the stock exchange, Obligation of REIT, Valuer and Sponsor, Disclosures, etc.

INTRODUCTION

The Securities and Exchange Board of India (SEBI) notified the Real Estate Investment Trusts (REITs) Regulations on 26 September 2014, thereby paving the way for introduction of an internationally acclaimed investment structure in India. The Finance Minister has also made necessary amendments to the Indian taxation regime to provide the tax pass through status, which is one of the key requirements for feasibility of REITs.

The Real estate Investment Trusts (REITs) Regulations, 2014, provide a positive push to the Indian Capital Markets and Real Estate & Infrastructure sectors. It also create liquidity to some extent for Real Estate and Infrastructure players. Further, it would provide investors an opportunity to invest in Indian stabilized assets through an Indian listed platform.

SEBI (REAL ESTATE INVESTMENT TRUST) REGULATIONS, 2014

“REIT” or “Real Estate Investment Trust” shall mean a trust registered as such under these regulations.

The activities of the Real Estate Investment Trust in the Indian capital market are regulated by SEBI (Real Estate Investment Trust) Regulations, 2014.

DEFINITIONS

“**Associate**” of any person includes shall be as defined under the Companies Act, 2013 or under the applicable accounting standards and shall also include following:-

- (i) Any person controlled, directly or indirectly, by the said person;
- (ii) Any person who controls, directly or indirectly, the said person;
- (iii) Where the said person is a company or a body corporate, any person(s) who is designated as promoter(s) of the company or body corporate and any other company or body corporate with the same promoter(s);
- (iv) Where the said person is an individual, any relative of the individual.

“**Floor Space Index**” or “**FSI**” shall mean the buildable area on a plot of land as specified by the competent authority.

“**Follow-On Offer**” means offer of units of a listed REIT to the public for subscription and includes an offer for sale of REIT units by an existing unit holder to the public;

“**Follow-On Offer Document**” means any document by which follow-on offer is made to the public;

“**Holdco**” or “**holding company**” shall mean a company or LLP, –

- (i) in which REIT holds or proposes to hold controlling interest and not less than fifty one per cent of the equity share capital or interest and which in turn has made investments in other SPV(s), which ultimately hold the property(ies);
- (ii) which is not engaged in any other activity other than holding of the underlying SPV(s), holding of real estate/properties and any other activities pertaining to and incidental to such holdings.

“**Investment Management Agreement**” means an agreement between the trustee and the manager which lays down the roles and responsibilities of the manager towards the REIT;

“**Occupancy Certificate**” means a completion certificate, or such other certificate, as the case may be, issued by the competent authority permitting occupation of any property under any law for the time being in force;

“**Real Estate**” Or “**Property**” means land and any permanently attached improvements to it, whether leasehold

or freehold and includes buildings, sheds, garages, fences, fittings, fixtures, warehouses, car parks, etc. and any other assets incidental to the ownership of real estate but does not include mortgage.

Apart from the above, following captured within the above mentioned definition of infrastructure shall be considered under “real estate” or “property”, -

- (i) hotels, hospitals and convention centers, forming part of composite real estate projects, whether rent generating or income generating;
- (ii) common infrastructure” for composite real estate projects, industrial parks and Special Economic Zone;

“Real Estate Assets” means properties owned by REIT whether directly or through a holdco and/or special purpose vehicle;

“Re-Designated Sponsor” means any person who has assumed the responsibility of the sponsor as provided under regulation 11 from the person as designated under clause (zt) of sub-regulation (1) i.e., Sponsor, of this regulation or from any re-designated sponsor thereafter;

“REIT Assets” means real estate assets and any other assets owned by the REIT whether directly or through a special purpose vehicle;

“Related Party” shall be defined under the Companies Act, 2013 or under the applicable accounting standards and shall also include:

- (i) parties to the REIT;
- (ii) sponsors, directors and partners of the persons in clause (i).

“Rent Generating Property” means property which has been leased or rented out in accordance with an agreement entered into for the purpose;

“Right-Of-First-Refusal” or **“ROFR”** of a REIT means the right given to the REIT by a person to enter into a transaction with it before the person is entitled to enter that transaction with any other party.

“Sponsor Group” – includes:

- (i) the sponsor(s);
- (ii) in case the sponsor is a body corporate:
 - (a) entities or person(s) which are controlled by such body corporate;
 - (b) entities or person(s) who control such body corporate;
 - (c) entities or person(s) which are controlled by person(s) as referred at clause b.
- (iii) in case sponsor is an individual:
 - (a) an immediate relative of such individual (i.e., any spouse of that person, or any parent, brother, sister or child of the person or of the spouse); and
 - (b) entities or person(s) which are controlled by such individual;

“Transferable Development Rights” or **“TDR”** shall mean development rights issued by the competent authority under relevant laws in lieu of the area relinquished or surrendered by the owner or developer or by way of declared incentives by the government or authority;

“Under-Construction Property” means a property of which construction is not complete and occupancy certificate has not been received;

“Valuer” means any person who is a “registered valuer” under section 247 of the Companies Act, 2013 or as defined hereunder and who has/have been appointed by the manager to undertake both financial and technical valuation of the REIT assets:

- (a) a valuer in respect of financial valuation, means,-
 - (i) a chartered accountant, company secretary or cost accountant who is in whole-time practice, or retired member of Indian Corporate Law Service or any person holding equivalent Indian or foreign qualification as the Ministry of Corporate Affairs may recognize by an order. However, such foreign qualification is acquired by Indian citizen.
 - (ii) a Merchant Banker registered with SEBI, and who has in his employment person(s) having qualifications prescribed under (i) above to carry out valuation by such qualified persons;
- (b) a valuer in respect of technical asset valuation, means members of the following institutions for specific asset categories,-
 - (i) Institution of Valuers;
 - (ii) Institution of Surveyors (Valuation Branch);
 - (iii) Institution of Government Approved Valuers;
 - (iv) Practicing Valuers Association of India;
 - (v) Centre for Valuation Studies, Research and Training;
 - (vi) Royal Institution of Chartered Surveyors, UK;
 - (vii) American Society of Appraisers, United States;
 - (viii) Appraisal Institute, United States;
 - (ix) Institute of Engineers;
 - (x) Council of Architecture or the Indian Institute of Architects;

However, the persons referred to in sub-sub-clause (i) and qualified person referred to in sub-sub-clause (ii) of sub-clause (a) above, shall have not less than five years continuous experience after acquiring membership of respective institutions.

Further that, the persons referred to in sub-sub-clauses (i) to (x) of sub-clause (b) above, shall have a minimum working experience of five years in relevant areas of valuation practice and in relation to relevant asset value and categories and be citizens of India.

REGISTRATION OF REAL ESTATE INVESTMENT TRUSTS

Any person shall not act as a REIT unless it is registered with SEBI under these regulations. An application for grant of certificate of registration as REIT shall be made, by the sponsor on behalf of the trust in such form and on such fees as prescribed in these regulations.

SEBI may, in order to protect the interests of investors, appoint any person to take charge of records, documents of the applicant and for this purpose, also determine the terms and conditions of such an appointment. SEBI shall take into account requirements as prescribed in these regulations for the purpose of considering grant of registration.

ELIGIBILITY CRITERIA

For the purpose of the grant of certificate to an applicant, SEBI shall consider all matters relevant to the activities as a REIT, namely, –

- (a) **Applicant** : The applicant is the sponsor on behalf of trust and the instrument of trust is in the form of a deed duly registered in India under the provisions of the Registration Act, 1908;
- (b) **Sponsor**: Each sponsor shall hold or propose to hold not less than 5% of the number of units of the REIT on post-initial offer basis. Each sponsor and sponsor group shall be clearly identified in the application of registration to SEBI and in the offer document/placement memorandum, as applicable. However, for each sponsor group not less than one person shall be identified as a sponsor.
- (c) **Manager**: It must have net worth of not less than Rs. 10 crore; not less than 5 years of experience in fund management/ advisory services/ property management in the real estate industry or in development of real estate; and not less than 2 key personnel who each have not less than 5 years of experience in fund management/ advisory services/ property management in the real estate industry or in development of real estate.
- (d) **Trustee**: It should be registered with SEBI under SEBI (Debenture Trustees) Regulations, 1993; not an associate of the sponsor/ manager/ principal valuer and the trustee has such wherewithal with respect to infrastructure, personnel, etc. to the satisfaction of SEBI.
- (e) The unit holder of the REIT shall not enjoys superior voting or any other rights over another unit holder and there are no multiple classes of units of REIT; Apart from the above, subordinate units may be issued only to the sponsors and its associates, where such subordinate units shall carry only inferior voting or any other rights compared to other units;
- (f) The applicant has clearly described details related to proposed activities at the time of application for registration.
- (g) The applicant and parties to the REIT shall be fit and proper persons.
- (h) Whether any previous application for grant of certificate by the applicant or any related party has been rejected by SEBI.
- (i) Whether any disciplinary action has been taken by SEBI or any other regulatory authority against the applicant or any related party under any Act or regulations or circulars etc.

PROCEDURE FOR GRANT OF CERTIFICATE

SEBI on being satisfied that the applicant fulfils the eligibility requirements, shall send intimation to the applicant and grant certificate of registration after receipt of the payment of registration fees as prescribed in these regulations,

CONDITIONS OF CERTIFICATE

The certificate granted as above shall, *inter-alia*, be subject to the following conditions, namely,-

The REIT shall abide by the provisions of the Act and these regulations;

The REIT shall forthwith inform SEBI in writing, if any information or particulars previously submitted to SEBI are found to be false or misleading in any material particular or if there is any material change in the information already submitted;

The REIT and parties to the REIT shall satisfy with the conditions as prescribed in these regulations;

The REIT and parties to the REIT shall comply with the Code of conduct.

PROCEDURE WHERE REGISTRATION IS REFUSED

After considering an application made by applicant, if SEBI is of the opinion that a certificate should not be granted to the applicant, it may reject the application after giving the applicant a reasonable opportunity of being heard. The decision of SEBI to reject the application shall be communicated to the applicant within 30 days of such decision.

ISSUE AND LISTING OF UNITS

ISSUE AND ALLOTMENT OF UNITS

1. A REIT shall make an initial offer of its units by way of public issue only.
2. No initial offer of units by the REIT shall be made unless,-

	the REIT shall be registered with SEBI under SEBI (Real Estate Investment Trusts) Regulations, 2014
	the value of all the assets owned by REIT is not less than 500 crore rupees;
	the minimum number of unit holders other than sponser(s), its related parties and its associates forming part of public shall be not less than 200.
	the offer size is not less than 250 crore rupees.

Note :

The requirement of ownership of assets and size of REIT may be complied at any point of time before allotment of units in accordance with offer document/placement memorandum subject to a binding agreement with the relevant party(ies). Such requirements shall be fulfilled prior to such allotment of units and, a declaration to SEBI and to the designated stock exchanges to that effect and adequate disclosures in this regard in the offer document.

3. For an REIT raising funds through an initial offer, the units proposed to be offered to the public through such initial offer:
 - (a) shall be not less than twenty five per cent of the total of the outstanding units of the REIT and the units being offered by way of the offer document, if the post issue capital of the REIT calculated at offer price is less than rupees one thousand six hundred crore;

However, the requirement at sub-clause (a) shall be complied along with the requirement under sub-regulation (2) of this Regulation.

- (b) shall be of the value of at least Rs 400 crore, if the post issue capital of the REIT calculated at offer price is equal to or more than rupees one thousand six hundred crore and less than rupees four thousand crore;
- (c) shall be not less than ten per cent of the total of the outstanding units of the REIT and the units being offered by way of the offer document, if the post issue capital of the REIT calculated at offer price is equal to or more than rupees four thousand crore;

However, any units offered to sponsor or the manager or their related parties or their associates shall not be counted towards units offered to the public.

Further that any listed REIT which has public holding below twenty five per cent on account of sub-clauses above, such REIT shall increase its public holding to at least twenty five per cent, within a period of three years from the date of listing pursuant to initial offer.

4. Any subsequent issue of units by the REIT may be by way of follow-on offer, preferential allotment, qualified institutional placement, rights issue, bonus issue, offer for sale or any other mechanism and in the manner as may be specified by SEBI.
5. REIT, through the merchant banker, shall file a draft offer document along with the fees specified in Schedule II with the designated stock exchange(s) and SEBI, not less than 30 working days before filing offer document with the designated stock exchange and SEBI.
6. The draft offer document filed with SEBI shall be made public, for comments, by hosting it on the websites of SEBI, designated stock exchanges and merchant bankers associated with the issue for a period of not less than 21 days.
7. The draft offer document and/or final offer document shall be accompanied by a due diligence certificate signed by lead merchant banker.
8. SEBI may communicate its comments to the lead merchant banker and, in the interest of investors, may require the lead merchant banker to carry out such modifications in the draft offer document as it deems fit.
9. The lead merchant banker shall ensure that all comments received from SEBI on the draft offer document are suitably taken into account prior to the filing of the offer document with the designated stock exchanges.
10. In case no observations are issued by SEBI in the draft offer document within 21 working days, then REIT may file the offer document or follow-on offer document with SEBI and the exchange(s).
11. The offer document shall be filed with the designated stock exchanges and SEBI not less than 5 working days before opening of the offer.
12. The initial offer or follow-on offer or right issue shall be made by the REIT within a period of not more than one year from the date of issuance of observations by SEBI.

However, if the initial offer or follow-on offer or right issue is not made within the specified time period, a fresh draft offer document shall be filed.

13. The REIT may invite for subscriptions and allot units to any person, whether resident or foreign. In case of foreign investors, such investment shall be subject to guidelines as may be specified by RBI and the government from time to time.
14. The application for subscription shall be accompanied by a statement containing the abridged version of the offer document, detailing the risk factors and summary of the terms of issue.

15. Under both the initial offer and follow-on public offer, the REIT shall not accept subscription of an amount less than two lakh rupees from an applicant.
16. Initial offer and follow-on offer shall not be open for subscription for a period of more than thirty days.
17. In case of over-subscriptions, the REIT shall allot units to the applicants on a proportionate basis rounded off to the nearest integer subject to minimum subscription amount per subscriber as specified above.
18. The REIT shall allot units or refund application money as the case may be, within twelve working days from the date of closing of the issue.
19. The REIT shall issue units only in dematerialized form to all the applicants.
20. The price of REIT units issued by way of public issue shall be determined through the book building process or any other process in accordance with the circulars or guidelines issued by SEBI and in the manner as may be specified by SEBI.
21. The REIT shall refund money to, -

(a) all applicants in case it fails to collect subscription amount of exceeding 90% of the fresh issue size as specified in the offer document

(b) applicants to the extent of oversubscription in case the moneys received is in excess of the extent of over-subscription as specified in the offer document.

(c) all applicants in case the number of subscribers to the initial offer forming part of the public is less than 200.

Note: - In case of Clause (b), right to retain such over subscription cannot exceed twenty five percent of the issue size. Further, that the offer document shall contain adequate disclosures towards the utilisation of such oversubscription proceeds, if any, and such proceeds retained on account of oversubscription shall not be utilised towards general purposes.

22. If the manager fails to allot, or list the units, or refund the money within the specified time, then the manager shall pay interest to the unit holders at 15% per annum, till such allotment/ listing/refund and such interest shall not be recovered in the form of fees or any other form payable to the manager by the REIT.
23. Units may be offered for sale to public:-
 - a) If such units have been held by the existing unit holders for a period of at least one year prior to the filing of draft offer document with SEBI.

However, the holding period for the equity shares or partnership interest in the holdco and/or SPV against which such units have been received shall be considered for the purpose of calculation of one year period.
 - b) Subject to other circulars or guidelines as may be specified by SEBI in this regard.

24. The amount for general purposes, as mentioned in objects of the issue in the draft document filed with SEBI, shall not exceed to 10 per cent of the amount raised by the REIT by issuance of units.
25. If the REIT fails to make its initial offer within three years from the date of registration with SEBI, it shall surrender its certificate of registration to SEBI and cease to operate as a REIT. SEBI if it deems fit, may extend the period by another one year. Further, the REIT may later re-apply for registration, if it so desires.
26. SEBI may specify by issue of guidelines or circulars any other requirements, as it deems fit, pertaining to issue and allotment of units by a REIT.

GUIDELINES FOR PUBLIC ISSUE OF UNITS OF REITs

The following are guidelines issued by SEBI for public issue of units of REITs:-

- The Manager on behalf of the REITs, 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.
- After receipt of comments from public and observations from SEBI, the draft offer document shall be filed with SEBI and the designated stock exchanges.
- In an issue made through the book building process or otherwise, the allocation in the public issue shall be as follows:
 - (a) not more than 75% to Institutional Investors
 - (b) not less than 25% to other investors
- The manager on behalf of the REIT, may allocate upto 60% of the portion available for allocation to Institutional Investors to anchor investors.
- The Manager on behalf of the REIT shall deposit, before the opening of subscription, and keep deposited with the stock exchange(s), an amount calculated at the rate of 0.5% of the amount of units offered for subscription to the public or Rs 5 crore, whichever is lower.
- A public issue shall be kept open for at least three working days but not more than thirty days.
- Where the REIT desires to have the issue underwritten, it shall appoint the underwriters in accordance with SEBI (Underwriters) Regulations, 1993.
- The manager on behalf of the REIT may determine the price of units in consultation with the merchant banker(s) or through the book building process.
- In all issues, the REIT shall accept bids including using ASBA facility, if so opted.
- On receipt of the sum payable on application, the manager on behalf of the REIT shall allot the units to the applicants.
- Records related to allocation process shall be maintained by the lead book runner and the book runner/s and other intermediaries associated in the book building process shall also maintain records of the book building prices.
- The merchant banker shall submit the following post-issue reports to SEBI:
 - (a) Initial post issue report, within three working days of closure of the issue.
 - (b) Final post issue report, within fifteen days of the date of finalization of basis of allotment or within fifteen days of refund of money in case of failure of issue.

- The merchant banker shall submit a due diligence certificate along with the final post issue report.
- Any public communication including advertisement, publicity material, research reports, etc. concerned with the issue shall not contain any matter extraneous to the contents of the draft offer document/offer document.
- The post-issue merchant banker(s) shall regularly monitor redressal of investor grievances relating to post-issue activities such as allotment, refund, etc.
- The post-issue merchant banker(s) shall ensure that advertisement giving details relating to oversubscription, basis of allotment, number, value and percentage of all applications, number, value and percentage of successful allottees for all applications, date of completion of dispatch of refund orders or instructions to Self Certified Syndicate Banks by the Registrar, date of dispatch of certificates and date of filing of listing application, etc. is released within ten days from the date of completion of the above activities on the website of the REIT, sponsor, manager, stock exchanges and in all the newspapers in which the pre issue advertisement was released, if applicable.
- The merchant bankers shall exercise due diligence and satisfy himself about all the aspects of the issue including the veracity and adequacy of disclosure in the offer documents.
- The merchant bankers shall ensure that the information contained in the offer document and the particulars as per audited financial statements in the offer document are not more than six months old from the issue opening date.

OFFER DOCUMENT AND ADVERTISEMENTS

The Offer document of the REIT shall contain material, true, correct and adequate disclosures to enable the investors to make an informed decision.

Without prejudice to the generality of above sub regulation, the offer document shall-

include disclosures for financial information of REIT as well as the Manager and the sponsor any circulars or guidelines issued by SEBI in this regard	not be misleading and not contain any untrue statements or mis-statements;	not provide for any guaranteed returns to the investors;	include such other disclosures as may be specified by SEBI
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Any advertisement material relating to any issue of units of the REIT shall not be misleading and shall not contain anything extraneous to the contents of the offer document. If an advertisement contains positive highlights, it shall also contain risk factors with equal importance in all aspects including print size.

The advertisements shall be in accordance with the offer document and any circulars or guidelines as may be specified by SEBI in this regard.

LISTING AND TRADING OF UNITS

1. After the initial offer it shall be mandatory for all units of REITs to be listed on a recognized stock exchange having nationwide trading terminals within a period of 12 working days from the date of closure of the offer.
2. The listing of the units of the REIT shall be in accordance with the listing agreement entered into between the REIT and the designated stock exchange.
3. In the event of non-receipt of listing permission from the stock exchange(s) or withdrawal of observation

Letter issued by SEBI, wherever applicable, the units shall not be eligible for listing and the REIT shall be liable to refund the subscription monies, if any, to the respective allottees immediately alongwith interest at the rate of fifteen per cent per annum from the date of allotment.

4. The units of the REIT listed in recognized stock exchanges shall be traded, cleared and settled in accordance with the bye-laws of concerned stock exchanges and such conditions as may be specified by SEBI.
5. Trading lot for the purpose of trading of units of the REIT shall be one lakh rupees.
6. The REIT shall redeem units only by way of a buy-back or at the time of delisting of units.
7. The units of REIT shall be remain listed on the designated stock exchange unless delisted under these regulation.
8. The minimum public holding for the units of the listed REIT shall be in accordance with the above mentioned sub-regulation 3, failing which action may be taken as may be specified by SEBI and by the designated stock exchange including delisting of units.

However, in case of breach of the conditions specified in this sub-regulation, the trustee may provide a period of six months to the manager to rectify the same, failing which the manager shall apply for delisting of units accordance with these regulations.

9. Any person other than the sponsor(s) holding units of the REIT prior to initial offer shall hold the units for a period of not less than one year from the date of listing of the units subject to circulars or guidelines as may be specified by SEBI.
10. SEBI and designated stock exchanges may specify any other requirements pertaining to listing and trading of units of the REIT by issuance of guidelines or circulars.

DELISTING OF UNITS

1. The manager shall apply for delisting of units of the REIT to SEBI and the designated stock exchanges if,-
 - (a) The public holding falls below the specified limit under these regulations.
 - (b) If there are no projects or assets remaining under the REIT for a period exceeding six months and REIT does not propose to invest in any project in future. The period may be extended by further six months, with the approval of unit holders in the manner as specified in these regulation.
 - (c) SEBI or the designated stock exchanges require such delisting for violation of the listing agreement or these regulations or the Act;
 - (d) The sponsor(s) or trustee requests such delisting and such request has been approved by unit holders in accordance with regulation 22(6);
 - (e) Unit holders apply for such delisting in accordance with these regulations.
 - (f) SEBI or the designated stock exchanges require such delisting for violation of the listing agreement, these regulations or the Act or in the interest of the unit holders.
2. SEBI and the designated stock exchanges may consider such application for approval or rejection as may be appropriate in the interest of the unit holders.
3. SEBI, instead of requiring delisting of the units, if it deems fit, may provide additional time to the REIT or parties to the REIT to comply with regulations.

4. SEBI may reject the application for delisting and take any other action, as it deems fit, for violation of the listing agreement or these regulations or the Act.
5. The procedure for delisting of units of REIT including provision of exit option to the unit holders shall be in accordance with the listing agreement and in accordance with procedure as may be specified by SEBI and by the designated stock exchanges from time to time.
6. SEBI may require the REIT to wind up and sell its assets in order to redeem units of the unit holders for the purpose of delisting of units and SEBI may through circulars or guidelines specify the manner of such winding up or sale.
7. After delisting of its units, the REIT shall surrender its certificate of registration to SEBI and shall no longer undertake activity of a REIT.

However, the REIT and parties to the REIT shall continue to be liable for all their acts of omissions and commissions with respect to activities of the REIT notwithstanding such surrender.

INVESTMENT CONDITIONS, RELATED PARTY TRANSACTIONS, BORROWING AND VALUATION OF ASSETS

INVESTMENT CONDITIONS AND DISTRIBUTION POLICY

- The Investment by a REIT shall only be in holdco and/or SPVs or properties or securities or TDR in India and the investment strategy as detailed in the offer document as may be amended in accordance with these regulations.
- The REIT shall not invest in vacant land or agricultural land or mortgages other than mortgage backed securities. However, this shall not apply to any land which is contiguous and extension of an existing project being implemented in stages.
- The REIT may invest in properties through SPVs subject to the following,-
 - (a) no other shareholder or partner of the SPV shall have any rights that prevents the REIT from complying with the provisions of these regulations; and an agreement shall be entered into which such shareholders or partner to that effect prior to investment in the SPV;
 - (b) the manager, in consultation with the trustee, shall appoint the majority of not less than one authorized representative on the Board of directors or governing board of such SPVs;
 - (c) the manager shall ensure that in every meeting including annual general meeting of the SPV, the voting of the REIT is exercised.
- The REIT may invest in properties through holdco subject the following –
 - (a) the ultimate holding interest of the REIT in the underlying SPV(s) is not less than twenty six per cent;
 - (b) no other shareholder or partner of the holdco or the SPV(s) shall have any rights that prevent the REIT, the holdco or the SPV(s) from complying with the provisions of these regulations and an agreement shall be entered into with such shareholders or partners to that effect prior to investment in the holdco and/or SPVs;
 - (c) the manager, in consultation with the Trustee, shall appoints the majority of the Board of directors or governing board of the holdco and/or SPV(s);
 - (d) the manager shall ensure that in every meeting including annual general meeting of the holdco and/or SPV(s), the voting of the REIT is exercised;
- Not less than 8% of value of the REIT assets shall be invested in completed and rent generating properties subject to the following –

- (a) If the investment has been made through a holdco and/or SPV, whether by way of equity or debtor equity linked instruments or partnership interest, only the portion of direct investments in properties by such holdco and/or SPVs shall be considered under this sub-regulation.
- (b) If any project is implemented in stages, the part of the project which is completed and rent-generating shall be considered under this sub-regulation and the remaining portion including any contiguous land.
- Not more than 20% of value of the REIT assets shall be invested in assets other than as provided above and such other investment shall only be in,-

(a) Properties, which are:

- under-construction properties which shall be held by the REIT for not less than 3 years after completion;
- under-construction properties which are a part of the existing income generating properties owned by the REIT which shall be held by the REIT for not less than 3 years after completion;
- completed and not rent generating properties which shall be held by the REIT for not less than 3 years from date of purchase;

(b) Listed or unlisted debt of companies or body corporate in real estate sector. This shall not include any investment made in debt of the holdco and/or SPV.

(c) Mortgage Backed Securities;

(d) Equity shares of companies listed on a recognized stock exchange in India which derive not less than seventy five per cent of their operating income from real estate activity as per the audited accounts of the previous financial year;

(e) Government Securities

(f) Unutilized FSI of a project where it has already made investment;

(g) TDR acquired for the purpose of utilization with respect to a project where it has already made investment;

(h) Money Market Instruments or Cash equivalents.;

- The investment conditions as specified above shall be complied at the time of offer document and thereafter.
- Not less than 51% of the revenues of the REIT, holdco and the SPV, other than gains arising from disposal of properties, shall be, at all times, from rental, leasing and letting real estate assets or any other income incidental to the leasing of such assets.
- Not less than 75% of value of the REIT assets proportionately on a consolidated basis shall be rent generating.
- A REIT shall hold at least two projects, directly or through holdco and/or SPV, with not more than 60% of the value of the assets, proportionately on a consolidated basis, in one project.
- Conditions specified in above shall be monitored the on a half-yearly basis and at the time of acquisition of an asset. If such conditions are breached, then manager shall inform the same to the trustee and ensure that the conditions as specified in this regulation are satisfied within six months of such breach.

Further, the period may be extended by another six months subject to approval from investors in accordance with these regulations.

- A REIT shall hold any completed and rent generating property, whether directly or through holdco or SPV, for a period of not less than 3 years from the date of purchase of such property by the REIT or holdco or SPV.
- For any sale of property, whether by the REIT or holdco or the SPV or for sale of shares or interest in the SPV by the holdco or REIT exceeding 10% of the value of REIT assets in a financial year, the manager shall obtain approval from the unit holders in accordance with these regulations.
- A REIT shall not invest in units of other REITs.
- A REIT shall not undertake lending to any person. However, investment in debt securities shall not be considered as lending.
- With respect to investment in lease hold properties, the manager shall consider the remaining term of the lease, the objectives of the REIT, the lease profile of the REIT's existing real estate assets and any other factors as may be relevant, prior to making such investment.
- In case of any co-investment with any person(s) in any transaction,-
 - (a) The investment by the other person(s) shall not be at terms more favourable than those to the REIT;
 - (b) The investment shall not provide any rights to the person(s) which shall prevent the REIT from complying with the provisions of these regulations;
 - (c) The agreement with such person(s) shall include the minimum percentage of distributable cash flows that will be distributed and entitlement of the REIT to receive not less than pro rata distributions and mode for resolution of any disputes between the REIT and the other person(s).
- With respect to distributions made by the REIT and the holdco and/or SPV,-
 - (a) Not less than 90% of net distributable cash flows of the SPV shall be distributed to the REIT/holdco in proportion of its holding in the SPV subject to applicable provisions in the Companies Act, 2013 or the LLP Act, 2008;
 - (b) with regard to distribution of net distributable cash flows by the holdco to the REIT, subject to applicable provisions in the Companies Act, 2013 or the Limited Liability Partnership Act, 2008, the following shall be complied:
 - with respect to the cash flows received by the holdco from underlying SPVs, 100% of such cash

flows received by the holdco shall be distributed to the REIT; and

- with respect to the cash flows generated by the holdco on its own, not less than 90% of such net distributable cash flows shall be distributed by the holdco to the REIT;
 - (c) Not less than 90% of net distributable cash flows of the REIT shall be distributed to the unit holders;
 - (d) Such distributions shall be declared and made not less than once every six months in every financial year and shall be made not later than 15 days from the date of such declaration;
 - (e) If any property is sold by the REIT or holdco or SPV or if the equity shares or interest in the holdco/SPV are sold by the REIT, then –
 - (i) If the REIT proposes to reinvest sale proceeds into another property, it shall not be required to distribute any sale proceeds from such sale to the unit holders;
 - (ii) If the REIT proposes not to invest the sales proceeds made into any other property within a period of 1 year, it shall be required to distribute not less than 75% of the sales proceeds in accordance with clauses (a), (b), (c) and (d) of 90% sub-regulation 16;
 - (f) If the distributions are not made within 15 days of declaration, then the manager shall be liable to pay interest to the unit holders at the rate of 15% per annum till the distribution is made and such interest shall not be recovered in the form of fees or any other form payable to the manager by the REIT.
- No schemes shall be launched under the REIT.
 - SEBI may specify any additional conditions for investments by the REIT as it deems fit.

RELATED PARTY TRANSACTIONS

- All related party transactions shall be on an arms-length basis, in the best interest of the unit holders, consistent with the strategy and investment objectives of the REIT and shall be disclosed to the designated stock exchange and unit holders periodically in accordance with the listing regulations and these regulations.

BORROWINGS AND DEFERRED PAYMENTS

- The aggregate consolidated borrowings and deferred payments of the REIT, holdco and/or the SPV(s), net of cash and cash equivalents shall never exceed 49% of the value of the REIT assets. However, such borrowings and deferred payments shall not include any refundable security deposits to tenants.
- If the aggregate consolidated borrowings and deferred payments of the REIT, holdco and/or the SPV(s) net of cash and cash equivalents exceed 25% of the value of the REIT assets, for any further borrowing,-
 - (a) Credit rating shall be obtained from a credit rating agency registered with SEBI; and
 - (b) Approval of unit holders shall be obtained in the manner as prescribed in these regulations.
- If the conditions specified above are breached on account of market movements of the price of the underlying assets or securities, the manager shall inform the same to the trustee and ensure that the conditions shall be satisfied within six months of such breach.

VALUATION OF ASSETS

- The valuer shall not be an associate of the sponsor(s) or manager or trustee and shall have not less than five years of experience in valuation of real estate.

- Full valuation includes a detailed valuation of all assets by the valuer including physical inspection of every property by the valuer.
- Full valuation report shall include the mandatory minimum disclosures as specified in Schedule V to these regulations.
- A full valuation shall be conducted by the valuer at least once in every financial year. However, such full valuation shall be conducted at the end of the financial year ending March 31st within three months from the end of such year.
- A half yearly valuation of the REIT assets shall be conducted by the valuer for the half year ending on September 30 for incorporating any key changes in the previous six months and such half yearly valuation report shall be prepared within 45 days from the date of end of such half year.
- Valuation reports received by the manager shall be submitted to the designated stock exchange and unit holders within 15 days from the receipt of such valuation reports.
- Prior to any issue of units to the public, the valuer shall undertake full valuation of all the REIT assets and include a summary of the report in the offer document. Such valuation report shall not be more than six months old at the time of such offer.

Further, this shall not apply in cases where full valuation has been undertaken not more than six months prior to such issue and no material changes have occurred thereafter.

- For any transaction of purchase or sale of properties whether directly or through holdco and/or SPV(s),-
 - (a) If the transaction is a related party transaction, the valuation shall be in accordance with these regulations.
 - (b) If the transaction is not a related party transaction,;-
 - a full valuation of the specific property shall be undertaken by the valuer;
 - if, -
 - in case of a **purchase transaction**, the property is proposed to be purchased at a value greater than one hundred and ten per cent of the value of the property as assessed by the valuer;
 - in case of a **sale transaction**, the property is proposed to be sold at a value less than ninety per cent of the value of the property as assessed by the valuer,

approval of the unit holders shall be obtained in accordance with regulation as prescribed in the regulations.
- No valuer shall undertake valuation of the same property for more than four years consecutively. The valuer may be reappointed after a period of not less than two years from the date it ceases to be the valuer of the REIT.
- Any valuation undertaken by any valuer shall abide by international valuation standards and valuation standards as may be specified by Institute of Chartered Accountants of India (ICAI) for valuation of real estate assets. In case of any conflict, standards specified by ICAI shall prevail.
- In case of any material development that may have an impact on the valuation of the REIT assets, then manager shall require the valuer to undertake full valuation of the property under consideration within not more than two months from the date of such event and disclose the same to the trustee, investors and the Designated Stock Exchanges within fifteen days of such valuation.
- The valuer shall not value any assets in which it has either been involved with the acquisition or disposal

within the last twelve months other than such cases where valuer was engaged by the REIT for such acquisition or disposal.

RIGHTS AND MEETINGS OF UNIT HOLDERS

1. The unit holder shall have the rights to receive income or distributions as provided for in the Offer document or trust deed.
2. With respect to any matter requiring approval of the unit holders,-
 - (a) a resolution shall be considered as passed when the votes cast by unit holders, so entitled and voting, in favour of the resolution exceed a certain percentage, as specified in this regulation, of the votes cast against;
 - (b) the voting may also be done by postal ballot or electronic mode;
 - (c) a notice of not less than 21 days either in writing or through electronic mode shall be provided to the unit holders;
 - (d) voting by any person who is a related party in such transaction as well as associates of such person(s) shall not be considered on the specific issue;
 - (e) manager shall be responsible for all the activities pertaining to conducting of meeting of the unit holders, subject to overseeing by the trustee.

However, In case of issue related to manager such as change in manager including removal of the manager or change in control of the manager, then trustee shall convene and handle all activities pertaining to conduct of the meetings.

Further, in case of issues related to trustee such as change in the trustee, the trustee shall not be involved in any manner in the conduct of the meeting.

3. An annual meeting of all unit holders shall be held not less than once a year within 120 days from the end of financial year and the time between two meetings shall not exceed 15 months.
4. With respect to the annual meeting of unit holders,-
 - (a) any information which is required to be disclosed to the unit holders and any issue, in the ordinary course of business, may require approval of the unit holders may be taken up in the meeting including,-
 - latest annual accounts and performance of the REIT;
 - approval of auditor and fees of such auditor, as may be required;
 - latest valuation reports;
 - appointment of valuer, as may be required;
 - any other issue including special issues as specified
 - (b) For any issue taken up in such meetings which require approval from the unit holders, votes cast in favour of the resolution shall be more than the votes cast against the resolution.
5. In case of,-
 - any approval from unit holders required for investment conditions, related party transactions and valuation of assets under these regulation;
 - any transaction, other than any borrowing, value of which is equal to or greater than 25% of the REIT assets;

- any borrowing in excess of specified limit as required under these regulations;
- any issue of units after initial offer by the REIT, in whatever form, other than any issue of units which may be considered by SEBI under sub regulation (6);
- increasing period for compliance with investment conditions to one year in accordance with these regulations.
- any issue, in the ordinary course of business, which in the opinion of the sponsor(s) or trustee or manager, is material and requires approval of the unit holders, if any;
- any issue for which SEBI or the designated stock exchange requires approval under this sub-regulation,

approval from unit holders shall be required where the votes cast in favour of the resolution shall be more than the votes cast against the resolution.

6. In case of , -

- (a) any change in manager including removal of the manager or change in control of the manager;
- (b) any material change in investment strategy or any change in the management fees of the REIT;
- (c) the sponsor(s) or manager proposing to seek delisting of units of the REIT;
- (d) the value of the units held by a person along with its associates other than the sponsor(s) and its associates exceeding fifty per cent of the value of outstanding REIT units, prior to acquiring any further units;
- (e) any issue, not in the ordinary course of business, which in the opinion of the sponsor(s) or manager or trustee requires approval of the unit holders;
- (f) any issue for which SEBI or the designated stock exchanges requires approval under this sub-regulation;
- (g) any issue taken up on request of the unit holders including:
 - removal of the manager and appointment of another manager to the REIT;
 - removal of the auditor and appointment of another auditor to the REIT;
 - removal of the valuer and appointment of another valuer to the REIT;
 - delisting of the REIT if the unit holders have sufficient reason to believe that such delisting would act in the interest of the unit holders;
 - any issue which the unit holders have sufficient reason to believe that acts detrimental to the interest of the unit holders;
 - change in the trustee if the unit holders have sufficient reason to believe that acts of such trustee is detrimental to the interest of the unit holders,

approval from unit holders shall be required where the votes cast in favour of the resolution shall be not less than one and half times the votes cast against the resolution.

However, in case of clause (d), if approval is not obtained, the person shall provide an exit option to the unit holders to the extent and in the manner as may be specified by SEBI.

7. With respect to the right(s) of the unit holders under clause (g) of sub-regulation (6), -

- (a) not less than 25% of the unit holders by value, other than any party related to the transactions and its associates, shall apply, in writing, to the trustee for the purpose;

- (b) on receipt of such application, the Trustee shall require the manager to place the issue for voting in the manner as specified in these regulations;
 - (c) with respect to sub-regulation (6)(g)(vi) , not less than 60% of the unit holders by value shall apply, in writing, to the manager for the purpose.
8. In case of any change in sponsor or re-designated sponsor or change in control of sponsor or re-designated sponsor,-
- prior to such changes, approval shall be obtained from the unit holders wherein votes cast in favour of the resolution shall not be less than three times the votes cast against the resolution;
 - if such change does not receive the required approval,-
 - (a) in case of change of sponsor or re-designated sponsor, the proposed re-designated sponsor who proposes to buy the units shall provide the dissenting unit holders an option to exit by buying their units;
 - (b) in case of change in control of the sponsor or re-designated sponsor, the sponsor or re-designated sponsor shall provide the dissenting unit holders an option to exit by buying their units;
 - If on account of such sale, the number of unit holders forming part of the public falls below two hundred or below, the trustee may provide a period of one year to the manager to rectify the same, failing, the manager shall apply for delisting of the units of the REIT in accordance with these regulations.

DISCLOSURES

- The manager shall ensure that the disclosures in the offer document are in accordance with these regulations and any circulars or guidelines issued by SEBI in this regard.
- The manager shall submit an annual report to all unit holders of the REIT with respect to activities of the REIT, within three months from the end of the financial year.
- The manager shall submit a half-yearly report to all unit holders of the REIT with respect to activities of the REIT within forty five days from the end of the half year ending on September 30th.
- Such annual and half yearly reports shall contain disclosures as specified under these regulations.
- The manager shall disclose to the designated stock exchanges, any information having bearing on the operation or performance of the REIT as well as price sensitive information which includes but is not restricted to the following,-
 - Acquisition or disposal of any properties, value of which exceeds 5% of value of the REIT assets;
 - Additional borrowing, at level of holdco or SPV or the REIT, resulting in such borrowing exceeding 5% of the value of the REIT assets during the year;
 - Additional issue of units by the REIT;
 - Details of any credit rating obtained by the REIT and any change in such rating;
 - Any issue which requires approval of the unit holders;
 - Any legal proceedings which may have significant bearing on the functioning of the REIT;
 - Notices and results of meetings of unit holders;
 - Any instance of non-compliance with these regulations including any breach of limits specified under these regulations;

- Any material issue that in the opinion of the manager or trustee needs to be disclosed to the unit holders.
- The manager shall submit such information to the designated stock exchanges and unit holders on a periodical basis as may be required under the listing agreement.
- The manager shall disclose to the designated stock exchanges, unit holders and SEBI such information and in the manner as may be specified by SEBI.

Regulation 23 prescribed that disclosures shall be made by a REIT as well as the Manager and the Sponsor to the Stock Exchange(s) where its units are listed. This said disclosures, inter-alia, include disclosures for financial as well as non-financial information. With reference to the aforesaid Regulations, the requirements for disclosure of financial information and pertinent compliances on continuous basis are placed at 'Annexure - A', and the requirements for disclosure of non-financial information and pertinent compliances on continuous basis are placed at 'Annexure - B'.

SUBMISSION OF REPORTS TO SEBI

SEBI may at any time call upon the REIT or parties to the REIT to file such reports, as SEBI may desire, with respect to the activities relating to the REIT.

POWER TO CALL FOR INFORMATION

SEBI may at any time call for any information from the REIT or parties to the REIT or any unit holder or any other person with respect to any matter relating to activity of the REIT. Where any information is called for, it shall be furnished within the time specified by SEBI.

MAINTENANCE OF RECORDS

- The manager shall maintain records pertaining to the activity of the REIT including for period of not less than seven years :
 - decisions of the manager with respect to investments or divestments and documents supporting the same;
 - details of investments made by the REIT and documents supporting the same;
 - agreements entered into by the REIT or on behalf of the REIT;
 - documents relating to appointment of persons as specified in regulation 10(5);
 - insurance policies for real estate assets;
 - investment management agreement;
 - documents pertaining to issue and listing of units including initial offer document or follow-on offer document(s) or other offer document(s), in-principle approval by designated stock exchanges, listing agreement with the designated stock exchanges, details of subscriptions, allotment of units, etc.;
 - distributions declared and made to the unit holders;
 - disclosures and periodical reporting made to the trustee, SEBI, unit holders and designated stock exchanges including annual reports, half yearly reports, etc.;
 - valuation reports including methodology of valuation;
 - books of accounts and financial statements;
 - audit reports;

- reports relating to activities of the REIT placed before the Board of Directors of the manager;
 - unit holders' grievances and actions taken thereon including copies of correspondences made with the unit holders and SEBI, if any;
 - any other material documents.
- The trustee shall maintain records pertaining to, –
- certificate of registration granted by SEBI;
 - registered trust deed;
 - documents pertaining to application made to SEBI for registration as a REIT;
 - titles of the real estate assets, where the original title documents are deposited with the lender in respect of any loan / debt, the trustee shall maintain copies of such title documents.
 - notices and agenda sent to unit holders for meetings held;
 - minutes of meetings and resolutions passed therein;
 - periodical reports and disclosures received by the trustee from the manager;
 - disclosures, periodically or otherwise, made to SEBI, unit holders and to the designated stock exchanges;
 - any other material documents.
- The records specified above, may be maintained in physical or electronic form. Where records are required to be duly signed and are maintained in the electronic form, such records shall be digitally signed.

LIABILITY FOR ACTION IN CASE OF DEFAULT

A REIT or parties to the REIT or any other person involved in the activity of the REIT who contravenes any of the provisions of the Act or these regulations, notifications, guidelines, circulars or instructions issued thereunder by SEBI shall be liable for one or more actions specified therein including any action provided under SEBI (Intermediaries) Regulations, 2008.

LESSON ROUND UP

- SEBI notified Real Estate Investment Trusts [REITs] Regulations to encourage and invests in real estate directly, either through properties or mortgages.
- REITs shall be set up as a trust and registered with SEBI. It shall have parties such as Trustee, Sponsor(s) and Manager.
- Rights and Responsibilities of Parties to the REIT, Valuer and Auditor shall be governed by SEBI (Real Estate Investment Trusts) Regulations, 2014.
- The REIT shall raise funds through an initial offer. Subsequent raising of funds may be through follow-on offer, rights issue, qualified institutional placement, etc.
- The Offer document of the REIT shall contain material, true, correct and adequate disclosures to enable the investors to make an informed decision.
- The advertisements shall be in accordance with the offer document and any circulars or guidelines as may be specified by SEBI in this regard.

Floor Space Index It means the buildable area on a plot of land as specified by the competent authority.

SELF TEST QUESTIONS

1. Explain major provisions of SEBI (Real Estate Investment Trusts) Regulation, 2014.
2. Discuss the Rights of Unit holders under SEBI (Real Estate Investment Trusts) Regulations, 2014.
3. Discuss the type of securities where REITs can invest its money and restrictions imposed as per the SEBI (Real Estate Investment Trusts) Regulation, 2014.
4. What are the eligibility criteria for approval of REITs? Explain the obligations and responsibilities of Sponsor as per SEBI (Real Estate Investment Trusts) Regulation, 2014.

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Lesson 15

Infrastructure Investment Trusts

LESSON OUTLINE

- Introduction
- SEBI (Infrastructure Investment Trusts) Regulations, 2014
- Registration of Infrastructure Investment Trusts
- Offer of Units of InvIT and Listing of Units
- Guidelines for Public Issue of units of InvITs
- Investment conditions, related party transactions, Borrowing and valuation of assets
- Rights and Meetings of Unit Holders
- Disclosures
- Inspection
- Liability for action in Case of Default
- LESSON ROUND UP
- GLOSSARY
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

Different Investment trusts are available to investor, one of them is Infrastructure Investment Trusts. Infrastructure Investment Trusts will be able to invest in infrastructure projects only; directly or through special purpose vehicles (SPVs).

The Securities and Exchange Board of India (SEBI) notified the Infrastructure Investment Trusts Regulations, 2014, which would provide an additional framework for investment in the infrastructure sectors in India.

In this lesson, the student will be able to learned and understand about the concept of InvIT, Registration of InvIT, Issue and listing of units in the stock exchange and Disclosures by InvITs etc.

INTRODUCTION

The Securities and Exchange Board of India (SEBI) notified the Infrastructure Investment Trusts Regulations on 26 September 2014, it examine a structure that would provide an additional framework for investment in the infrastructure sector in India. The Finance Minister has also made necessary amendments in the Indian taxation with respect to InvITs. Infrastructure Investment Trusts will be able to invest in infrastructure projects only directly or through special purpose vehicles (SPVs). For public-private partnership (PPP) projects, investments can be routed only be through an SPV.

SEBI (INFRASTRUCTURE INVESTMENT TRUSTS) REGULATIONS, 2014

“InvIT” or ‘Infrastructure Investment Trust’ shall mean the trust registered as such under these regulations.

The activities of the Infrastructure Investment Trusts in the Indian capital market are regulated by SEBI (Infrastructure Investment Trusts) Regulations, 2014.

DEFINITIONS

“**Governing board**” in case of an LLP shall mean a group of members assigned by the LLP to act in a manner similar to the board of directors in case of a company.

“**General Purposes**” include such identified purposes for which no specific amount is allocated or any amount so specified towards general purpose or any such purpose by whatever name called, in the draft offer document filed with SEBI.

However, any issue related expenses shall not be considered as a part of general purpose merely because no specific amount has been allocated for such expenses in the draft offer document filed with SEBI.

“**Infrastructure**” includes all infrastructure sub-sectors as defined vide notification of the Ministry of Finance dated October 07, 2013 and shall include any amendments or additions made thereof.

“**Completed and revenue generating project**” means an infrastructure project, which prior to the date of its acquisition by, or transfer to, the InvIT, satisfies the following conditions, the infrastructure project has -

- (i) achieved the commercial operations date as defined under the relevant project agreement including concession agreement, power purchase agreement or any other agreement of a similar nature entered into in relation to the operation of the project or in any agreement entered into with the lenders;
- (ii) received all the requisite approvals and certifications for commencing operations; and
- (iii) been generating revenue from operations for a period of not less than one year;

“**Concession Agreement**” means an agreement entered into by a person with a concessioning authority for the purpose of implementation of the project as provided in the agreement.

“**Concessioning Authority**” means the public sector concessioning authority in PPP projects.

“**Eligible Infrastructure Project**” means an infrastructure project which, prior to the date of its acquisition by, or transfer to, the InvIT, satisfies the following conditions,—

- For PPP projects,—
 - a) the Infrastructure Project is a completed and revenue generating project or
 - b) the Infrastructure Project, which has achieved commercial operations date and does not have the track record of revenue from operations for a period of not less than one year, or
 - c) the Infrastructure Project is a pre-COD project;

- In non-PPP projects, the infrastructure project has received all the requisite approvals and certifications for commencing construction of the project.

“Follow-On Offer” means offer of units of an InvIT to the public for subscription and includes an offer for sale of InvIT units by an existing unit holder to the public.

“Infrastructure Developer” in case of PPP projects shall mean the lead member of the concessionaire SPV.

“Investment Management Agreement” means an agreement between the trustee and the investment manager which lays down the roles and responsibilities of the investment manager towards the InvIT.

“PPP Project” means an infrastructure project undertaken on a Public-Private Partnership basis between a public concessioning authority and a private SPV concessionaire selected on the basis of open competitive bidding or on the basis of an MOU with the relevant authorities.

“Pre-Cod Project” means an infrastructure project which,–

- has not achieved commercial operation date as defined under the relevant project agreements including
 - the concession agreement,
 - power purchase agreement or
 - any other agreement of a similar nature entered into in relation to the operation of a project or
- any agreement entered into with the lenders; and
- has achieved completion of at least 50% of the construction of the infrastructure project as certified by an independent engineer of such project or expended not less than 50% of the total capital cost set forth in the financial package of the relevant project agreement.

“Project Implementation Agreement” or **“Project Management Agreement”** means an agreement between the project manager, the concessionaire SPV and the trustee which sets out obligations of the project manager with respect to execution of the project.

Though, in case of PPP projects, such obligations shall be in addition to the responsibilities as under the concession agreement or any such agreement entered into with the concessioning authority.

“SPV” Or “Special Purpose Vehicle” means any company or LLP,–

- in which either the InvIT or the holdco holds or proposes to hold controlling interest and not less than 51% of the equity share capital or interest.

However, in case of PPP projects where such acquiring or holding is disallowed by government or regulatory provisions under the concession agreement or such other agreement, this clause shall not apply and shall be apply subject to provisions under proviso to sub-regulation (3) of regulation 12.

- which holds not less than 90% of its assets directly in infrastructure projects and does not invest in other SPVs; and
- which is not engaged in any other activity other than activities pertaining to and incidental to the underlying infrastructure projects;

‘Strategic Investor’ means,–

- (a) An infrastructure finance company registered with RBI as a NBFC;
- (b) A Scheduled Commercial Bank;
- (c) An International Multilateral Financial Institution;

- (d) A systemically important NBFCs registered with RBI; and
- (e) A foreign portfolio investors.

who together invest not less than 5% the total offer size of the InvIT or such amount as may be specified by SEBI from time to time;

“Under-Construction Project” means an infrastructure project whether PPP or non-PPP, which :

- (a) has either not achieved commercial operation date as defined under the relevant project agreements including :
 - the concession agreement;
 - Power Purchase Agreement; or
 - any other agreement of a similar nature entered into in relation to the operation of a project; or
 - any agreement entered into with the lenders; or
- (b) has achieved commercial operation date and does not have the track record of revenue from operations for a period of not less than one year.

“InvIT assets” means assets owned by the InvIT, whether directly or through a holdco and/or SPV, and includes all rights, interests and benefits arising from and incidental to ownership of such assets.

“Value of the InvIT” means value of the InvIT as assessed by the valuer based on value of the infrastructure and other assets owned by the InvIT, whether directly or through SPV excluding any debtor liabilities thereof.

“Value Of InvIT Assets” means value of InvIT assets as assessed by the valuer based on value of the infrastructure and other assets owned by the InvIT, whether directly or through holdco and/or SPV.

REGISTRATION OF INFRASTRUCTURE INVESTMENT TRUSTS

Any person shall not act as an InvIT unless it has obtained a certificate of registration from the SEBI under these regulations. An application for grant of certificate of registration as InvIT shall be made by the sponsor on behalf of the trust in such form and in such a manner as prescribed in these regulations.

The SEBI may, in order to protect the interests of investors, appoint any person to take charge of records, documents of the applicant and for this purpose, also determine the terms and conditions of such an appointment. The SEBI shall take into account requirements as specified in these regulations for the purpose of considering grant of registration.

ELIGIBILITY CRITERIA

For the purpose of the grant of certificate to an applicant, the SEBI shall consider all matters relevant to the activities as an InvIT.

Without prejudice to the generality of the foregoing provisions, the SEBI shall consider the following, mandatory requirements namely,–

- a) **Applicant:** Applicant must be a sponsor on the behalf of Trust and the Trust deed must be duly registered in India under the provisions of the Registration Act, 1908 containing the main objective as undertaking activity of REIT in accordance with the set Regulations.
- b) **Sponsor:** Each sponsor shall be clearly identified in the application of registration to SEBI and in the offer document/ placement memorandum, as applicable. Each sponsor must have:-
 - Net worth of not less than Rs. 100 Crores if it is a body corporate or a company; or
 - Net tangible assets of value not less than Rs 100 crore in case it is a limited liability partnership.

- On a collective basis and have not less than 5 years' experience in the real estate industry on an individual basis.
- Sound track record in development of infrastructure or fund management in the infrastructure sector.

Explanation : For the purpose of this clause, 'sound track record' means experience of at least 5 years and where the sponsor is a developer, at least two projects of the sponsor have been completed;

c) **Investment Manager** : The Investment Manager has:-

- Net worth of not less than rupees 10 crore if the investment manager is a body corporate or a company or
- Net tangible assets of value not less than 10 crore rupees in case the investment manager is a limited liability partnership.
- Not less than 5 years' experience in fund management or advisory services or development in the infrastructure sector.
- Not less than 2 employees who have at least 5 years' experience each, in fund management or advisory services or development in the infrastructure sector;
- Not less than one employee who has at least 5 years' experience in the relevant subsector (s) in which the InvIT has invested or proposes to invest.
- Not less than half of its directors in case of a company or members of the governing board in case of an LLP as independent and not directors or members of the governing board of another InvIT;
- An office in India from where the operations pertaining to the InvIT is proposed to be conducted.
- Entered into an investment management agreement with the trustee which provides for the responsibilities of the investment manager in accordance with these regulations.

d) **Trustee**: It should be registered with SEBI under SEBI(Debt Trustees) Regulations, 1993; not an associate of the sponsor/ manager and the trustee has such wherewithal with respect to infrastructure, personnel, etc. to the satisfaction of SEBI and in accordance with circulars or guidelines as may be specified by SEBI;

e) The project manager has been identified and shall be appointed in terms of the project implementation/ management agreement. However, the project implementation agreement/ management agreement shall be submitted along with the draft offer document/ or the placement memorandum.

f) No unit holder of the InvIT enjoys superior voting or any other rights over another unit holder and there shall not be multiple classes of units of InvITs. Notwithstanding the above, subordinate units may be issued only to the sponsors and its associates, where such subordinate units shall carry only inferior voting or any other rights compared to other units;

g) The applicant has clearly described at the time of registration, details pertaining to proposed activities of the InvIT;

h) The applicant, sponsor(s), investment manager, project manager(s) and trustee are fit and proper persons based on the criteria as specified in SEBI(Intermediaries) Regulations, 2008;

i) Whether any previous application for grant of certificate made by the applicant or any related party has been rejected by the SEBI;

j) Whether any disciplinary action has been taken by the SEBI or any other regulatory authority against the applicant or any related party under any Act or the regulations or circulars or guidelines made thereunder.

PROCEDURE FOR GRANT OF CERTIFICATE

SEBI on being satisfied that the applicant fulfils, the requirements specified in these regulations, shall send intimation to the applicant and grant certificate of registration after receipt of registration fees as prescribed in the regulations.

However, the SEBI may grant in-principle approval to the applicants, where it deems fit and on satisfaction of all requirements as specified in these regulations, grant final registration to the applicant. The registration may be granted with such conditions as may be deemed appropriate by the SEBI.

CONDITIONS OF CERTIFICATE

The certificate granted under these regulations shall, inter-alia, be subject to the following conditions,-

The InvIT shall abide by the provisions of the Act and these regulations;

The InvIT shall forthwith inform the SEBI in writing, if any information or particulars previously submitted to SEBI are found to be false or misleading in any material particular or if there is any material change in the information already submitted;

The InvIT and parties to the InvIT shall satisfy with the eligibility criteria specified in these regulations at all times;

The InvIT and parties to the InvIT shall comply with the Code of conduct as specified in these regulations.

PROCEDURE WHERE REGISTRATION IS REFUSED

After considering an application of registration, if the SEBI is of the opinion that a certificate should not be granted to the applicant, it may reject the application after giving the applicant a reasonable opportunity of being heard. The decision of the SEBI to reject the application shall be communicated to the applicant within thirty days of such decision.

OFFER OF UNITS OF InvIT AND LISTING OF UNITS

ISSUE OF UNITS AND ALLOTMENT

- No initial offer of units by an InvIT shall be made unless,-
 - o The InvIT is registered with SEBI under these regulations;

- o The value of the assets held by the InvIT is not less than rupees five hundred crore.

Explanation – Such value shall mean the value of the specific portion of the holding of InvIT in the underlying assets or holdco or SPVs;

- o The offer size is not less than rupees two hundred fifty crore.

However, the requirement of ownership of assets under clause (b) and offer size under clause (c) may be complied at any point of time before allotment of units in accordance with offer document/ placement memorandum subject, to a binding agreement with the relevant party(ies) that such the requirements shall be fulfilled prior to such allotment and a declaration to SEBI and to the designated stock exchanges to that effect, where applicable and adequate disclosures in this regard in the offer document or placement memorandum.

- The minimum offer and allotment to public through an offer document/ placement memorandum shall be, –

- o atleast twenty five per cent of the total outstanding units of the InvIT, if the post issue capital of the InvIT calculated at offer price is less than rupees one thousand six hundred crore:

However, this requirement shall be complied along with the requirement under Regulation 14(1) (c) of the InvIT Regulations.

- o of the value of atleast Rs 400 crore, if the post issue capital of the InvIT calculated at offer price is equal to or more than rupees one thousand six hundred crore and less than rupees four thousand crore;

- o atleast ten per cent of the total outstanding units of the InvIT, if the post issue capital of the InvIT calculated at offer price is equal to or more than rupees four thousand crore.

However, any units offered to sponsor or the investment manager or the project manager or their related parties or their associates shall not be counted towards units offered to the public.

Further that any listed InvIT which has public holding below twenty five per cent on account of sub-clauses (b) and (c) above, such InvIT shall increase its public holding to at least twenty five per cent, within a period of three years from the date of listing pursuant to initial offer.

- If the InvIT, raises funds by way of private placement –

- a. it shall do it through a placement memorandum;
- b. from qualified institutional buyers and body corporate only, whether Indian or foreign.

However, in case of foreign investors, such investment shall be subject to guidelines as may be specified by RBI and the government from time to time;

- c. with minimum investment from any investor of rupees one crore;

“Apart the above, if such an privately placed InvIT invests or proposes to invest not less than eighty per cent of the value of the InvIT assets, the minimum investment from an investor shall be rupees twenty five crore;”

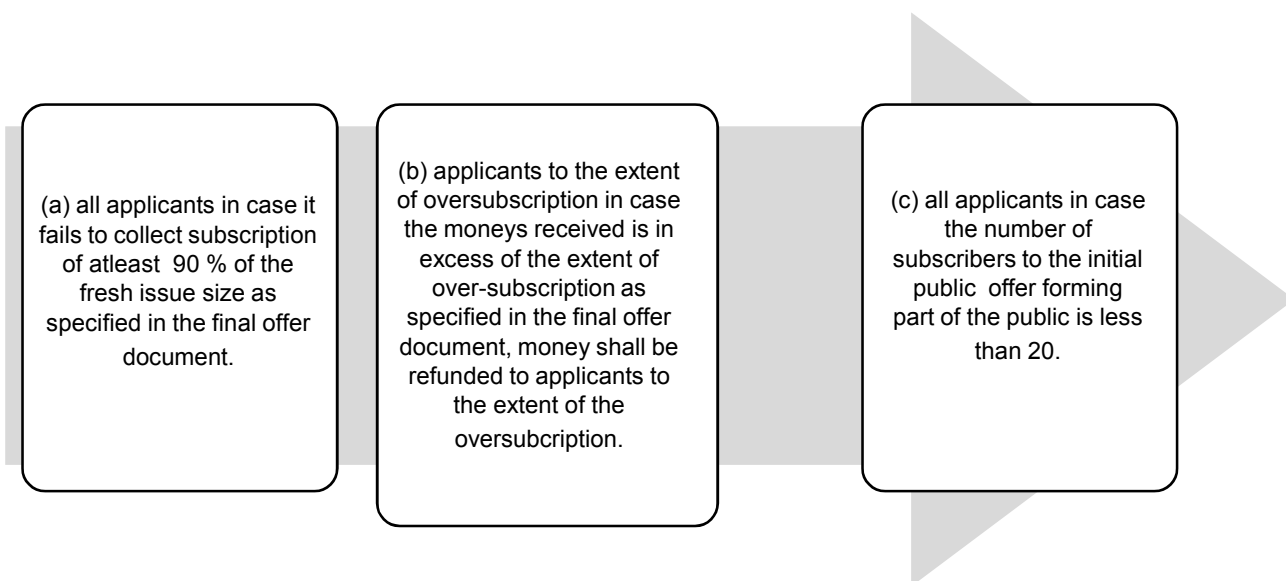
- d. from not less than five and not more than one thousand investors.
- e. shall file a placement memorandum with SEBI alongwith the fee as specified in Schedule II, atleast 5 days prior to opening of the issue.

However, such opening of the issue shall not be at a date later than 3 months from the receipt of in-principle approval for listing, from exchange(s).

– If the InvIT raises funds by public issue InvITs –

- it shall be by way of initial public offer ;
- any subsequent issue of units after initial public offer may be by way of follow-on offer, preferential allotment, qualified institutional placement, rights issue, bonus issue, offer for sale or any other mechanism and in the manner as may be specified by SEBI;
- minimum subscription from any investor in initial and follow-on offer shall be ten lakh rupees ;
- prior to initial public offer and follow-on offer, the merchant banker shall file the draft offer document along with the fee as specified in Schedule II, with the designated stock exchange(s) and SEBI not less than thirty working days before filing the offer document with the and SEBI;
- the draft offer document filed with SEBI shall be made public, for comments, if any, to be submitted to SEBI, within a period of at least ten days, by hosting it on the websites of SEBI, designated stock exchanges and merchant bankers associated with the issue for a period of not less than twenty one days.
- SEBI may communicate its comments to the lead merchant banker and, in the interest of investors, may require the lead merchant banker to carry out such modifications in the draft offer document as it deems fit;
- the lead merchant banker shall ensure that all comments received from SEBI on the draft offer document are suitably addressed prior to the filing of the offer document with the designated stock exchanges;
- in case no observations are issued by SEBI in the draft offer document within twenty one working days from the date of receipt of satisfactory reply from the lead merchant bankers or manager, the InvIT may file the offer document or follow on offer document with SEBI and the exchange(s);
- the draft and offer document shall be accompanied by a due diligence certificate signed by the lead merchant banker;
- the offer document shall be filed with the designated stock exchanges and SEBI not less than five working days before opening of the offer
- The InvIT may open the initial public offer or follow-on offer or rights issue within a period of not more than one year from the date of issuance of observations by SEBI. However, if the initial public offer or follow-on offer or rights issue is not made within the prescribed time period, a fresh draft offer document shall be filed.
- The InvIT may invite for subscriptions and allot units to any person, whether resident or foreign. However, in case of foreign investors, such investment shall be subject to guidelines as may be specified by RBI and the government from time to time.
- the application for subscription shall be accompanied by a statement containing the abridged version of the offer document detailing the risk factors and summary of the terms of issue;
- initial public offer and follow-on offer shall not be open for subscription for a period of more than thirty days;
- in case of over-subscriptions, the InvIT shall allot units to the applicants on a proportionate basis rounded off to the nearest integer subject to minimum subscription amount per subscriber as discussed above.
- the InvIT shall allot units or refund application money, as the case may be, within twelve working days from the date of closing of the issue;

- the InvIT shall issue units in only in dematerialized form to all the applicants;
- the price of InvIT units issued by way of public issue shall be determined through the book building process or any other process in accordance with the guidelines issued by SEBI and in the manner as may be specified by SEBI;
- the InvIT shall refund money, –



Note : In Clause (b) Further, that the offer document shall contain adequate disclosures towards the utilisation of such oversubscription proceeds, if any, and such proceeds retained on account of oversubscription shall not be utilised towards general purposes.

- If the investment manager fails to allot or list the units or refund the money within the specified time, then the investment manager shall pay interest to the unit holders at the rate of fifteen per cent per annum, till such allotment or listing or refund and such interest shall be not be recovered in the form of fees or any other form payable to the investment manager by the InvIT;
- units may be offered for sale to public,–
 - (i) if such units have been held by the sellers for a period of at least one year prior to the filing of draft offer document with SEBI. However, the holding period for the equity shares or partnership interest in the holdco or SPV against which such units have been received shall be considered for the purpose of calculation of one year period;
 - (ii) subject to other guidelines as may be specified by SEBI in this regard;
- The amount for general purposes, as mentioned in objects of the issue in the draft offer document filed with SEBI, shall not exceed ten per cent of the amount raised by the InvIT by issuance of units.

GUIDELINES FOR PUBLIC ISSUE OF UNITS OF InvITs

The following are guidelines issued by SEBI for public issue of units of InvITs:-

- The Investment Manager on behalf of the InvIT, 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.
- After receipt of comments from public and observations from SEBI, the draft offer document shall be filed with SEBI and the designated stock exchanges.

- In an issue made through the book building process or otherwise, the allocation in the public issue shall be as follows:
 - (a) not more than 75% to Institutional Investors
 - (b) not less than 25% to other investors
- Investment manager on behalf of the InvIT, may allocate upto 60% of the portion available for allocation to Institutional Investors to anchor investors.
- The Investment Manager on behalf of the InvIT, shall deposit, before the opening of subscription, and keep deposited with the stock exchange(s), an amount calculated at the rate of 0.5% of the amount of units offered for subscription to the public or Rs. 5 crore, whichever is lower.
- A public issue shall be kept open for at least three working days but not more than thirty days.
- Where the InvIT desires to have the issue underwritten, it shall appoint the underwriters in accordance with SEBI (Underwriters) Regulations, 1993.
- The investment manager on behalf of the InvIT, may determine the price of units in consultation with the lead merchant banker or through the book building process.
- In all issues, the InvIT shall accept bids including using ASBA facility, if so opted.
- On receipt of the sum payable on application, the investment manager on behalf of the InvIT shall allot the units to the applicants.
- Records related to allocation process shall be maintained by the lead book runner and the book runner/s and other intermediaries associated in the book building process shall also maintain records of the book building prices.
- The lead merchant banker shall submit the following post-issue reports to SEBI:
 - a) Initial post issue report, within three working days of closure of the issue.
 - b) Final post issue report, within fifteen days of the date of finalization of basis of allotment or within fifteen days of refund of money in case of failure of issue.
- The lead merchant banker shall submit a due diligence certificate along with the final post issue report.
- Any public communication including advertisement, publicity material, research reports, etc. concerned with the issue shall not contain any matter extraneous to the contents of the offer document.
- The post-issue lead merchant banker shall regularly monitor redressal of investor grievances relating to post-issue activities such as allotment, refund, etc.
- The post-issue merchant banker shall ensure that advertisement giving details relating to oversubscription, basis of allotment, number, value and percentage of all applications, number, value and percentage of successful allottees for all applications, date of completion of dispatch of refund orders or instructions to Self Certified Syndicate Banks by the Registrar, date of dispatch of certificates and date of filing of listing application, etc. is released within ten days from the date of completion of the above activities on the website of the InvIT, sponsor, investment manager, stock exchanges and in all the newspapers in which the pre issue advertisement was released, if applicable.
- The lead merchant bankers shall exercise due diligence and satisfy himself about all the aspects of the issue including the veracity and adequacy of disclosure in the offer documents.
- The lead merchant banker shall ensure that the information contained in the offer document and the particulars as per audited financial statements in the offer document are not more than six months old from the issue opening date.

OFFER DOCUMENT OR PLACEMENT MEMORANDUM AND ADVERTISEMENTS

The offer document or placement memorandum of the InvIT shall contain material, true, correct and adequate disclosures to enable the investors to make an informed decision.

Without prejudice to the generality of above sub regulation, the offer document or placement memorandum shall –		
not be misleading and not contain any untrue statements or mis-statements;	not provide for any guaranteed returns to the investors;	include such other disclosures as may be specified by SEBI

The offer document and placement memorandum shall include all information as specified under Schedule III of these regulations.

No advertisement shall be issued pertaining to issue of units by an InvIT which makes a private placement of its units.

With respect to advertisements pertaining to the offer of units by an InvIT with respect to public issue of its units,-

- such advertisement material shall not be misleading and shall not contain anything extraneous to the contents of the offer document;
- if an advertisement contains positive highlights, it shall also contain risk factors with equal importance in all aspects including print size;
- the advertisements shall be in accordance with any circulars or guidelines as may be specified by SEBI in this regard.

LISTING AND TRADING OF UNITS

- It shall be mandatory for units of all InvITs to be listed on a recognized stock exchange having nationwide trading terminals, whether publicly issued or privately placed.

However, this sub-regulation shall not apply if the initial offer does not satisfy the minimum subscription amount or the minimum number of subscribers under these regulations.

- The listing of the units shall be in accordance with the listing agreement entered into between the InvIT and the designated stock exchanges.
- In the event of non-receipt of listing permission from the stock exchange(s) or withdrawal of observation Letter issued by SEBI, wherever applicable, the units shall not be eligible for listing and the InvIT shall be liable to refund the subscription monies, if any, to the respective allottees immediately alongwith interest at the rate of fifteen per cent per annum from the date of allotment.
- The units of the InvIT listed in the designated stock exchanges shall be traded, cleared and settled in accordance with the bye-laws of designated stock exchanges and such conditions as may be specified by SEBI.
- The InvIT shall redeem units only by way of a buyback or at the time of delisting of units.
- The units shall remain listed on the designated Stock Exchanges unless delisted under these regulations.
- The minimum public holding for the units of the InvIT after listing shall be, in accordance with regulation of issue of units and allotment failing which action may be taken as may be specified by SEBI and by the

designated stock exchanges including delisting of units under these regulations.

- The minimum number of unit holders in an InvIT other than the sponsor, its related parties and its associates (s) ,–
 - o in case of privately placed InvIT, shall be five, each holding not more than 25% of the units of the InvIT.
 - o forming part of public shall be twenty, each holding not more than 25% of the units of the InvIT, at all times post listing of the units, failing which action may be taken as may be specified by SEBI and by the designated stock exchanges including delisting of units under these regulations.
- With respect to listing of privately placed units,–
 - o its units shall be mandatorily listed on the designated stock exchange(s) within twelve working days from the date of allotment. However, this sub-regulation shall not apply if the initial offer does not satisfy the minimum subscription amount or the minimum number of subscribers as prescribed in these regulations.
 - o trading lot for the purpose of trading of units on the designated stock exchange shall be five lakh rupees.

Apart the above, if an InvIT invests not less than eighty per cent of the value of the InvIT assets, the trading lot for the purpose of trading of units on the designated stock exchange of such InvIT shall be rupees two crore.
- With respect to listing of publicly offered units,–
 - o Its units shall be mandatorily listed on the designated stock exchange(s) within 12 working days from the date of closure of the initial public offer. This sub-regulation shall not apply if the initial public offer does not satisfy the minimum subscription amount or the minimum number of subscribers as prescribed in these regulations.
 - o Trading lot for the purpose of trading of units on the designated stock exchange shall be five lakh rupees.
- Any person other than the sponsor(s) holding units of the InvIT prior to initial offer shall hold the units for a period of not less than one year from the date of listing of the units.
- SEBI and designated stock exchanges may specify any other requirements pertaining to listing and trading of units of the InvIT by issuance of guidelines or circulars.

DELISTING OF UNITS AND WINDING UP OF THE InvIT

- The investment manager shall apply for delisting of units of the InvIT to SEBI and the designated stock exchanges if, –

(a) the public holding falls below the specified limit under these regulations.

(b) the number of unit holders of the InvIT falls below the limit as prescribed in these regulations.

(c) if there are no projects or assets remaining under the InvIT for a period exceeding six months and InvIT does not propose to invest in any project in future.

(d) SEBI or the designated stock exchanges require such delisting for violation of the listing agreement or these regulations or the Act;

(e) the sponsor(s) or trustee requests such delisting and such request has been approved by unit holders in accordance with these regulations.

(f) unit holders apply for such delisting in accordance with these regulations

(g) SEBI or the designated stock exchanges require such delisting in the interest of the unit holders.

Note:-

- In Clause (c), the period may be extended by further 6 months, with the approval of unit holders in the manner as prescribed in these regulations.
- If clause (a) or (b) is breached, the trustee may provide a period of six months to the investment manager to rectify the same, failing which shall apply for such delisting.
- In case of PPP projects, such delisting shall be subject to relevant clauses in the concession agreement.
- SEBI and the designated stock exchanges may consider such application for delisting for approval or rejection as may be appropriate in the interest of the unit holders.
- SEBI may, instead of delisting of the units, if it deems fit, provide additional time to the InvIT or parties to the InvIT to comply with above mentioned conditions.
- SEBI may reject the application for delisting and take any other action, as it deems fit, under these regulations or the Act for violation of the listing agreement or these regulations or the Act.
- The procedure for delisting of units of InvIT including provision of exit option to the unit holders shall be in accordance with the listing agreement and in accordance with procedure as may be specified by SEBI and by the designated stock exchanges from time to time.
- After delisting of its units, the InvIT shall surrender its certificate of registration to SEBI and shall no longer undertake activity of an InvIT.
- The InvIT and parties to the InvIT shall continue to be liable for all their acts of omissions and commissions with respect to activities of the InvIT notwithstanding surrender of registration to SEBI.

INVESTMENT CONDITIONS, RELATED PARTY TRANSACTIONS, BORROWING AND VALUATION OF ASSETS

INVESTMENT CONDITIONS AND DIVIDEND POLICY

- The investment by an InvIT shall only be in holdco and/ or SPVs or infrastructure projects or securities in India in accordance with these regulations and the investment strategy as detailed in the offer document or Placement memorandum.
- In case of PPP projects, the InvIT shall mandatorily invest in the infrastructure projects through holdco and/ or SPV.
- The InvIT may invest in infrastructure projects through SPVs subject to the following,–

- a. in case the SPV is a company/LLP, the investment manager, in consultation with the trustee, shall appoint not less than one authorized representative on majority of the board of directors or governing board of such SPVs as applicable;
 - b. in case the SPV is a company, the investment manager, in consultation with the trustee, shall appoint not less than one authorized representative on the board of directors or governing board of such SPVs ;
 - c. the investment manager shall ensure that in every meeting including annual general meeting of the SPV, the voting of the InvIT is exercised.
- The InvIT may invest in infrastructure projects through holdcos subject to the following,-
 - a. the ultimate holding interest of the InvIT in the underlying SPV(s) is not less than twenty six per cent;
 - b. no other shareholder or partner of the holdco or the SPV(s) shall have any rights that prevent the InvIT, the holdco or the SPV(s) from complying with the provisions of these regulations and an agreement shall be entered into with such shareholders or partners to that effect prior to investment in the holdco/SPV;
 - c. the investment manager, in consultation with the Trustee, shall appoint the majority of the Board of directors or governing board of the holdco and SPV(s);
 - d. the investment manager shall ensure that in every meeting including annual general meeting of the holdco and SPV(s), the voting of the InvIT is exercised;
 - In case of InvIT as specified under these regulation, the InvIT shall invest not less than eighty per cent of the value of the InvIT assets in eligible infrastructure projects either directly or through holdcos or through SPVs. However, un-invested funds may be invested in instruments as provided under sub-clause (ii), (iii), (iv) and (v) of clause (b) of sub-regulation 5 of this regulation.
 - In case of InvITs as specified above in these regulations,-
 - a) not less than 8% of the value of the InvIT assets shall be invested, proportionate to the holding of the InvITs, in completed and revenue generating infrastructure projects subject to the following;
 - (i) if the investment has been made through a holdco and/ or SPV(s), whether by way of equity or debt or equity linked instruments or partnership interest, only the portion of direct investments in completed and revenue generating projects by such holdco and/ or SPV(s) shall be considered under this sub regulation and the remaining portion shall be included under clause (b);
 - (ii) if any project is implemented in stages, the part of the project which can be categorized as completed and revenue generating project shall be considered under this sub-regulation and the remaining portion shall be included under clause (b);
 - b) not more than twenty per cent of value of the InvIT assets, shall be invested in,—
 - i. under construction infrastructure projects, whether directly or through holdco and/ or SPVs.
However, investment in such assets shall not exceed ten per cent of the value of the InvIT assets;
 - ii. listed or unlisted debt of companies or body corporate in infrastructure sector. However, this shall not include any investment made in debt of the holdco and/ or SPV(s).
 - iii. equity shares of companies listed on a recognized stock exchange in India which derive not less than eighty per cent of their operating income from infrastructure sector as per the audited accounts of the previous financial year;

- iv. government securities;
- v. money market instruments, liquid mutual funds or cash equivalents;
- c) if the conditions specified in clauses (a) and (b) are breached, the investment manager shall inform the same to the trustee and ensure that the conditions as specified in this regulation are satisfied within six months of such breach. However, the period may be extended to one year subject to approval from investors in accordance with these regulations.
- The investment conditions as specified at sub-regulation (4) and (5) of this regulation and sub-regulation shall be complied at the time of Offer document/placement memorandum and thereafter.
- With respect to distributions made by the InvIT and the holdco and/or SPV,-
 - a. not less than ninety per cent of net distributable cash flows of the SPV shall be distributed to the InvIT/holdco in proportion of its holding in the SPV subject to applicable provisions in Companies Act, 2013 or Limited Liability Partnership Act, 2008;
 - b. not less than ninety per cent of net distributable cash flows of the InvIT shall be distributed to the unit holders;
 - c. with regard to distribution of net distributable cash flows by the holdco to the InvIT, the following shall be complied:
 - (i) with respect to the cash flows received by the holdco from underlying SPVs, 100% of such cash flows received by the holdco shall be distributed to the InvIT; and
 - (ii) with respect to the cash flows generated by the holdco on its own, not less than 90% of such net distributable cash flows shall be distributed by the holdco to the InvIT.
 - d. such distributions shall be declared and made not less than once every six months in every financial year in case of publicly offered InvITs and not less than once every year in case of privately placed InvITs and shall be made not later than fifteen days from the date of such declaration;
 - e. subject to sub-clause (c), such distribution shall be as per the dates and in the manner as mentioned in the offer document or placement memorandum.
- If any infrastructure asset is sold by the InvIT or holdco or SPV or if the equity shares or interest in the holdco/SPV are sold by the InvIT,-
 - a. if the InvIT proposes to re-invest the sale proceeds into another infrastructure asset , it shall not be required to distribute any sales proceeds to the InvIT or to the investors;
 - b. If the InvIT proposes not to invest the sales proceeds into any other infrastructure asset within a period of one year, it shall be requiring to distribute the same in accordance with above sub-regulation.
- If the distributions are not made within fifteen days of declaration, then the investment manager shall be liable to pay interest to the unit holders at the rate of fifteen per cent per annum till the distribution is made and such interest shall be not be recovered in the form of fees or any other form payable to the investment manager by the InvIT.
- An InvIT shall not invest in units of other InvITs.
- An InvIT shall not undertake lending to any person other than the holdco/ SPV(s) in which the InvIT has invested in. However, investment in debt securities shall not be considered as lending.
- An InvIT shall hold an infrastructure asset for a period of not less than three years from the date of purchase of such asset by the InvIT, directly or through holdco and/or SPV. However, this shall not apply to investment in securities of companies in infrastructure sector other than SPVs.

- In case of any co-investment with any person(s) in any transaction,—
 - a. the investment by the other person(s) shall not be at terms more favourable than those to the InvIT;
 - b. the investment shall not provide any rights to the person(s) which shall prevent the InvIT from complying with the provisions of these regulations;
 - c. the agreement with such person(s) shall include the minimum percentage of distributable cash flows that will be distributed and entitlement of the InvIT to receive not less than pro rata distributions and mode for resolution of any disputes between the InvIT and the other person(s).
- No schemes shall be launched under the InvIT.
- SEBI may specify any additional conditions for investments by the InvIT as deemed fit.

RELATED PARTY TRANSACTIONS

- All related party transactions shall be on an arms-length basis in accordance with relevant accounting standards, in the best interest of the unit holders, consistent with the strategy and investment objectives of the InvIT.

BORROWINGS AND DEFERRED PAYMENTS

- The aggregate consolidated borrowings and deferred payments of the InvIT, holdco and the SPV(s), net of cash and cash equivalents shall never exceed forty nine per cent of the value of the InvIT assets.
- If the aggregate consolidated borrowings and deferred payments of the InvIT, holdco and the SPV(s), net of cash and cash equivalents exceed twenty five per cent of the value of the InvIT assets, for any further borrowing, —
 - (a) credit rating shall be obtained from a credit rating agency registered with SEBI and
 - (b) approval of unit holders shall be obtained in the manner as prescribed in the regulations.
- If the conditions specified above, are breached on account of market movements of the price of the underlying assets or securities, the investment manager shall inform the same to the trustee and ensure that the conditions are satisfied within six months of such breach.

VALUATION OF ASSETS

- The valuer shall not be an associate of the sponsor(s) or investment manager or trustee and shall have not less than five years of experience in valuation of infrastructure assets.
- Full valuation includes a detailed valuation of all assets of the InvIT by the valuer including physical inspection of every infrastructure project by the valuer.
- Full valuation report shall include the mandatory minimum disclosures as specified in Schedule V.
- A full valuation shall be conducted by the valuer not less than once in every financial year. However, such full valuation shall be conducted at the end of the financial year ending March 31st within two months from the date of end of such year.
- A half yearly valuation of the assets of the InvIT shall be conducted by the valuer for the half-year ending September 30th for a publicly offered InvIT for incorporating any key changes in the previous six months and such half yearly valuation report shall be prepared within one month from the date of end of such half year.
- Valuation reports received by the investment manager shall be submitted by the investment manager to the designated stock exchanges within fifteen days from the receipt of such valuation reports.

- Prior to any issue of units by publicly offered InvIT other than bonus issue, the valuer shall undertake full valuation of all the InvIT assets and include the same in the Offer Document.

However, such valuation report shall not be more than six months old at the time of such offer.

Further that this shall not apply in cases where full valuation has been undertaken not more than six months prior to such issue and no material changes have occurred thereafter.

- For any transaction of purchase or sale of infrastructure projects, whether directly or through holdco and/or SPVs, for publicly offered InvITs,—
 - a full valuation of the specific project shall be undertaken by the valuer;
 - if,—
 - (a) in case of a **Purchase Transaction**, the asset is proposed to be purchased at a value greater than hundred ten per cent of the value of the asset as assessed by the valuer;
 - (b) in case of a **Sale Transaction**, the asset is proposed to be sold at a value less than ninety per cent of the value of the asset as assessed by the valuer, approval of the unit holders shall be obtained in accordance with these regulations.
- No valuer shall undertake valuation of the same project for more than four years consecutively. However, the valuer may be reappointed after a period of not less than two years from the date it ceases to be the valuer of the InvIT.
- Any valuation undertaken by any valuer shall be in compliance with by international valuation standards and valuation standards as may be specified by Institute of Chartered Accountants of India for valuation of infrastructure assets or such other valuation standards as may be specified by SEBI. However, in case of any conflict, standards specified by Institute of Chartered Accountants of India shall prevail.
- In case of any material development that may have an impact on the valuation of the assets of the InvIT, then investment manager of a publicly offered InvIT shall require the valuer to undertake full valuation of the infrastructure project under consideration within not more than two months from the date of such event and disclose the same to the trustee and the designated stock exchanges within fifteen days of such valuation.
- The valuer shall not undertake valuation of any assets in which it has either been involved with the acquisition or disposal within the last twelve months other than such cases where the valuer was engaged by the InvIT for such acquisition or disposal.

RIGHTS AND MEETINGS OF UNIT HOLDERS

1. The unit holder shall have the rights to receive income or distributions as provided for in the offer document or placement memorandum.
2. With respect to any matter requiring approval of the unit holders,—
 - a resolution shall be considered as passed when the votes cast by unit holders, so entitled and voting, in favour of the resolution exceed a certain percentage as specified in these regulations, of votes cast against;
 - the voting may also be done by postal ballot or electronic mode;
 - a notice of not less than twenty one days shall be provided to the unit holders;

- voting by any person who is a related party in such transaction as well as associates of such person(s) shall not be considered on the specific issue;
- investment manager shall be responsible for all the activities pertaining to conducting of meeting of the unit holder, subject to overseeing by the trustee.

However, in issues pertaining to the investment manager such as change in investment manager including removal of the investment manager or change in control of the investment manager, trustee shall convene and handle all activities pertaining to conduct of the meetings.

Further that in respect of issues pertaining to the trustee including change in the trustee, the trustee shall not be involved in any manner in the conduct of the meeting.

3. For an InvITs,–

- an annual meeting of all unit holders shall be held not less than once a year within one hundred twenty days from the end of financial year and the time between two meetings shall not exceed fifteen months;
- with respect to the annual meeting of unit holders, –
 - any information that is required to be disclosed to the unit holders and any issue that, in the ordinary course of business, may require approval of the unit holders may be taken up in the meeting including, –
 - (a) latest annual accounts and performance of the InvIT;
 - (b) approval of auditor and fees of such auditor, as may be required;
 - (c) latest valuation reports;
 - (d) appointment of valuer, as may be required;
 - (e) any other issue;
 - for any issue taken up in such meetings which require approval from the unit holders other than as specified in sub-regulation (6) under, votes cast in favour of the resolution shall be more than the votes cast against the resolution;

4. In case of,–

- any approval from unit holders required for investment conditions, related party transactions and valuation of assets.
- any transaction, other than any borrowing, value of which is equal to or greater than twenty five per cent of the InvIT assets;
- any borrowing in excess of specified limit as required above in borrowing and deferred payment regulation;
- any issue of units after initial public offer by an InvIT, in whatever form, other than any issue of units which may be considered by SEBI under sub-regulation (5);
- increasing period for compliance with investment conditions to one year in accordance with these regulations.

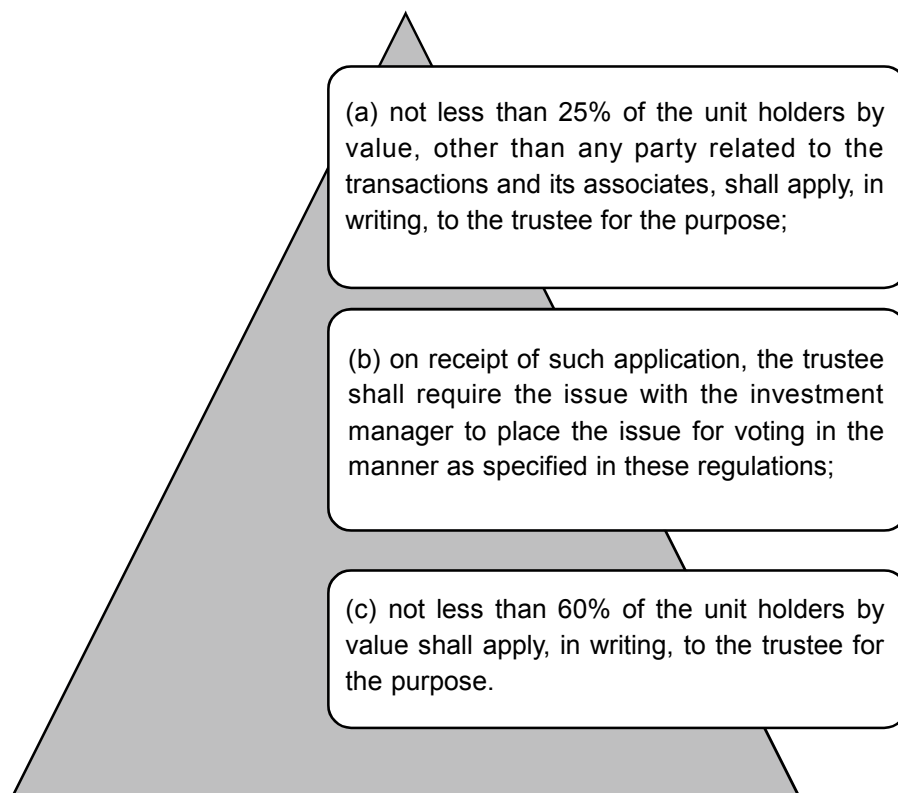
- any issue, in the ordinary course of business, which in the opinion of the sponsor(s) or trustee or investment manager, is material and requires approval of the unit holders, if any;
- any issue for which SEBI or the designated stock exchanges requires such approval under this sub-regulation, approval from unit holders shall be required where votes cast in favour of the resolution shall be more than the votes cast against the resolution.

5. In case of, –

- any change in investment manager including removal of the investment manager or change in control of the investment manager;
- any material change in investment strategy or any change in the management fees of the InvIT.
- the sponsor(s) or investment manager proposing to seek delisting of units of the InvIT.
- any issue, not in the ordinary course of business, which in the opinion of the sponsor(s) or investment manager or trustee requires approval of the unit holders;
- any issue for which SEBI or the designated stock exchanges requires approval under this sub-regulation;
- any issue taken up on request of the unit holders including,–
 - removal of the investment manager and appointment of another investment manager to the InvIT;
 - removal of the auditor and appointment of another audit or to the InvIT;
 - removal of the valuer and appointment of another valuer to the InvIT;
 - delisting of an InvIT, if the unit holders have sufficient reason to believe that such delisting would act in the interest of the unit holders;
 - any issue which the unit holders have sufficient reason to believe that is detrimental to the interest of the unit holders;
 - change in the trustee if the unit holders have sufficient reason to believe that acts of such trustee is detrimental to the interest of the unit holders;
 - approval from unit holders shall be required where votes cast in favour of the resolution shall not be less than one and a half times the votes cast against the resolution.

However, in case of above clause, if approval is not obtained, the person shall provide an exit option to the unit holder to the extent and in the manner specified by SEBI.

6. With respect to the right(s) of the unit holders under above clauses of sub-regulation (5),–



DISCLOSURES

- A privately placed InvIT shall ensure that the disclosures in the placement memorandum are in accordance with these regulations and any circulars or guidelines issued by SEBI in this regard.
- A publicly offered InvIT shall ensure that the disclosures in the offer document are in accordance with the Schedule III and any circulars or guidelines issued by SEBI in this regard.
- The investment manager of all InvITs shall submit an annual report to all unit holders electronically or by physical copies and to the designated stock exchanges within three months from the end of the financial year.
- The investment manager of shall submit a half-yearly report to the designated stock exchange within forty five days from the end of the every half year ending March 31st and September 30th.
- Such annual and half yearly reports shall contain disclosures as specified under Schedule IV.
- The investment manager shall disclose to the designated stock exchanges any information having bearing on the operation or performance of the InvIT as well as price sensitive information which includes but is not restricted to the following,–
 - Acquisition or disposal of any projects, directly or through holdco or SPV, value of which exceeds 5% of value of the InvIT assets;
 - Additional borrowing, at level of holdco or SPV or the InvIT, exceeding fifteen per cent of the value of the InvIT assets ;

- Additional issue of units by the InvIT;
 - Details of any credit rating obtained by the InvIT and any change in such rating;
 - Any issue which requires approval of the unit holders;
 - Any legal proceedings which may have significant bearing on the functioning of the InvIT;
 - Notices and results of meetings of unit holders,
 - Any instance of non-compliance with these regulations including any breach of limits specified under the regulations;
 - Any material issue that in the opinion of the investment manager or trustee needs to be disclosed to the unit holders.
- The InvIT shall also submit such information to the designated stock exchanges and unit holders on a periodical basis as may be required under the listing agreement.
 - The InvIT shall disclose to the designated stock exchanges, unit holders and SEBI such information and in the manner as may be specified by SEBI.
 - The InvIT shall also provide disclosures or reports specific to sector or sub-sector in which the InvIT has invested or proposes to invest in the manner as may be specified by SEBI.
 - The InvIT shall made disclosures to the stock exchange(s) where its units are listed. The said disclosures *inter alia*, include disclosure for financial as well as non-financial information.

SUBMISSION OF REPORTS TO SEBI

SEBI may at any time call upon the InvIT or parties to the InvIT to file such reports, as SEBI may desire, with respect to the activities relating to the InvIT.

MAINTENANCE OF RECORDS

- The investment manager shall maintain records pertaining to the activity of the InvIT, wherever applicable, including,–
 - all investments or divestments of the InvIT and documents supporting the same including rationale for such investments or divestments;
 - agreements entered into by the InvIT or on behalf of the InvIT;
 - documents relating to appointment of persons as specified in regulation 10(5).
 - insurance policies for infrastructure assets;
 - investment management agreement;
 - documents pertaining to issue and listing of units including placement memorandum, draft and final offer document, in-principle approval by designated stock exchanges, listing agreement with the designated stock exchanges, details of subscriptions, allotment of units, etc;
 - distributions declared and made to the unit holders;
 - disclosures and periodical reporting made to the trustee, SEBI, unit holders and the designated stock exchanges including annual reports, half yearly reports, etc.;

- valuation reports including methodology of valuation;
 - books of accounts and financial statements;
 - audit reports;
 - reports relating to activities of the InvIT placed before the board of directors of the investment manager;
 - unit holders' grievances and actions taken thereon including copies of correspondences made with the unit holder and SEBI, if any;
 - any other material documents;
- The trustee shall maintain records, wherever applicable, pertaining to,–
- certificate of registration granted by SEBI;
 - registered trust deed;
 - documents pertaining to application made to SEBI for registration as an InvIT;
 - titles of the infrastructure assets, where the original title documents are deposited with the lender or any other person in respect of any loan or debt, the trustee shall maintain copies of such title documents;
 - notices and agenda sent to unit holders for meetings held;
 - minutes of meetings and resolutions passed therein;
 - periodical reports and disclosures received by the trustee from the investment manager;
 - disclosures, periodically or otherwise, made to SEBI, unit holders and the designated stock exchanges;
 - any other material documents.
- The aforesaid records may be maintained in physical or electronic form. However, where records are required to be duly signed and are maintained in the electronic form, such records shall be digitally signed.

INSPECTION

SEBI RIGHT TO INSPECT

SEBI may *suo motu* or upon receipt of information or complaint appoint one or more persons as inspecting officers to undertake inspection of the books of accounts, records and documents relating to activity of the InvIT or holdco or SPV or parties to the InvIT for any of the following reasons, namely,–

- (a) to ensure that the books of account, records and documents are being maintained by the InvIT or parties to the InvIT in the manner specified in these regulations;
- (b) to inspect into complaints received from unit holders, clients or any other person, on any matter having a bearing on the activities of the InvIT;
- (c) to ascertain whether the provisions of the Act and these regulations are being complied with by the InvIT and parties to the InvIT; and
- (d) to inspect *suo motu* into the affairs of the InvIT, in the interest of the securities market or in the interest of investors.

OBLIGATION OF INVIT, PARTIES TO THE INVIT AND ANY OTHER ASSOCIATE PERSONS ON INSPECTION

- It shall be the duty of every InvIT in respect of whom an inspection has been ordered, parties to the InvIT and any other associate person who is in possession of relevant information pertaining to conduct and affairs of such InvIT, including :-
 - representative of InvIT, if any, to produce to the inspecting officer such books, accounts and other documents in his custody or control and
 - furnish him with such statements and information as the inspecting officer may require for the purposes of inspection.
- It shall be the duty of every InvIT, parties to the InvIT and any other associate person give all such assistance and co-operation as may be required in connection with the inspection to Inspecting officer and to furnish such information as may be sought by the inspecting officer in connection with the inspection.
- The inspecting officer shall, for the purposes of inspection, have power to examine on oath and record the statement of any employees and directors of the InvIT or parties to the InvIT or any person responsible for or connected with the activities of InvIT or any other associated person having relevant information pertaining to such InvIT.
- The inspecting officer shall, for the purposes of inspection, have power to obtain authenticated copies of documents, books, accounts of InvIT, from any person having control or custody of such documents, books or accounts.

COMMUNICATION OF FINDINGS ETC. TO THE INVIT

SEBI may after consideration of the inspection report and after giving reasonable opportunity of hearing to the InvITs or parties to the InvIT or its representatives or any such person, issue such directions as it deems fit in the interest of securities market or the investors in the nature of,–

- requiring the InvIT to delist its units from the stock exchanges and surrender its certificate of registration;
- requiring the InvIT to wind up;
- requiring the InvIT to sell its assets;
- requiring the InvIT or parties to the InvIT to take such action as may be in the interest of the investors;
- prohibiting the InvIT or parties to the InvIT from operating in the capital market or from accessing the capital market for a specified period.

LIABILITY FOR ACTION IN CASE OF DEFAULT

An InvIT or parties to the InvIT or any other person involved in the activity of the InvIT who contravenes any of the provisions of the Act or these regulations or notifications, guidelines, circulars or instructions issued thereunder by SEBI shall be liable for one or more actions specified therein including any action provided under SEBI (Intermediaries) Regulations, 2008.

LESSON ROUND UP

- SEBI notified Infrastructure Investment Trusts Regulations, to encourage and invests in infrastructure projects only directly or through Special Purpose Vehicles.
- InvIT shall mean the trust registered as such under these regulations. It shall have parties such as Trustee, Sponsor(s) and Investment Manager.
- The InvITs can raise capital from both domestic and foreign investors. Raising capital from foreign investor pursuant to initial offer of units or follow-on offer can be made.
- The offer document or placement memorandum of the InvIT shall contain material, true, correct and adequate disclosures to enable the investors to make an informed decision.
- The advertisements shall be in accordance with the offer document and any circulars or guidelines as may be specified by SEBI in this regard.
- The Investment Manager shall submit to the trustee, quarterly reports on the activities of the InvIT including receipts for all funds received by it and for all payments made, position on compliance with these regulations, specifically compliance with investment conditions, related parties transactions and borrowing and deferred payments, performance report, status of development of under-construction projects, within thirty days of end of such quarter.
- The Investment Manager shall submit valuation reports received to the designated stock exchanges within fifteen days from the receipt of such valuation reports.
- The records may be maintained in physical or electronic form. However, if records are maintained in electronic form it shall be digitally signed.
- An InvIT or parties to the InvIT or any other person involved in the activity of the InvIT who contravenes any of the provisions of the Act or these regulations or notifications, guidelines, circulars or instructions issued thereunder by SEBI shall be liable for one or more actions specified therein including any action provided under SEBI (Intermediaries) Regulations, 2008.

GLOSSARY

Concession Agreement	An agreement entered into by a person with a concessioning authority for the purpose of implementation of the project as provided in the agreement;
IMA	Investment management Agreement is an agreement between the trustee and the investment manager which lays down the roles and responsibilities of the manager towards the InvIT;
ROFR	"Right-Of-First-Refusal" of a REIT means the right given to the REIT by a person to enter into a transaction with it before the person is entitled to enter that transaction with any other party.

SELF TEST QUESTIONS

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation)

1. Discuss the procedure relating to inspection of Infrastructure Investment Trusts.
2. Explain major provisions of SEBI (Infrastructure Investment Trusts) Regulation, 2014.
3. What are the obligations of Investment Manager under SEBI (Infrastructure Investment Trusts) Regulations, 2014?

4. Discuss the type of securities in which InvIT can invest as per the SEBI (Infrastructure Investment Trusts) Regulation, 2014.
5. What are the eligibility criteria for approval of InvITs?
6. Explain the obligations and responsibilities of Sponsor under these regulations.

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Lesson 16

Regulatory Framework Governing Stock Exchanges

LESSON OUTLINE

- Introduction
- Securities Contracts (Regulation) Act, 1956
- Corporatisation and Demutualisation of Stock Exchanges
- Procedure for corporatisation and demutualisation
- Contracts in Securities
- Public Issue and Listing of Securities
- Penalties and Procedures
- Offences
- Rights of Investors
- Securities Contract (Regulation) (Stock Exchange and Clearing Corporations) Regulations, 2012
- Securities Contracts (Regulation) Rules, 1957
- Requirements of listing of securities with recognised stock exchanges
- Continuous Listing Requirement
- Delisting of securities
- LESSON ROUND UP
- GLOSSARY
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

Stock Market plays a significant role in development of Economy. Stock Market facilitates mobilization of funds from small investors and channelizes these resources into various development needs of various sectors of the economy. In order to prevent undesirable transactions in securities by regulating the business of dealing therein, and by providing for certain other matters connected therewith, the Securities Contracts (Regulation) Act, 1956 was enacted by Parliament.

After going through this lesson, the student will be able to know about the Powers of Stock Exchange and SEBI under the SCRA Act, the penal provisions, procedures, offences, procedure for appeal to SAT, Right of Investors, Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporations) Regulations, 2012 and Securities Contract (Regulation) Rules, 1957 etc.

INTRODUCTION

The Securities Contracts (Regulation) Act, 1956 provides for direct and indirect control of all aspects of the securities trading including the running of stock exchanges which aims to prevent undesirable transaction in securities. It gives the Central Government regulatory jurisdiction over (a) Stock exchanges through a process of recognition and continued supervision, (b) contracts in securities, and (c) listing of securities on stock exchanges. As a condition of recognition, a stock exchange complies with the requirements prescribed by the Central Government. The stock exchange frame their own listing regulations in consonance with the minimum listing criteria set out in Securities contracts (Regulation) Rules, 1957.

The Government promulgated the Securities Contracts (Regulation) Rules, 1957 for carrying into effect the objects of the Securities Contracts (Regulation) Act. These rules provide among other things, for the procedure to be followed for recognition of Stock Exchanges; Submission of periodical returns and annual reports by recognised stock exchanges; inquiry into the affairs of stock exchanges and their members; and requirements for listing of securities. The rules are statutory and they constitute a code of standardised regulations uniformly applicable to all the recognised stock exchanges.

SEBI also issued the Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporations) Regulations, 2012 to regulate the recognition, ownership and governance in stock exchanges and clearing corporations.

SECURITIES CONTRACTS (REGULATION) ACT, 1956

The Securities Contracts (Regulation) Act, 1956 was enacted by Parliament to prevent undesirable transactions in securities by regulating the business of dealing therein, by providing for certain other matters connected therewith. The Act extends to the whole of India and came into force on 28th February, 1957. The Act defines various terms in relation to securities and provides the detailed procedure for the stock exchanges to get recognition from Government/SEBI, procedure for listing of securities of companies and operations of the brokers in relation to purchase and sale of securities on behalf of investors.

However, the provisions of this Act shall not apply to –

- (a) the Government, the Reserve Bank of India, any local authority or any corporation set up by a special law or any person who has effected any transaction with or through the agency of any such authority as is referred to in this clause;
- (b) any convertible bond or share warrant or any option or right in relation thereto, in so far as it entitles the person in whose favour any of the foregoing has been issued to obtain at his option from the company or other body corporate, issuing the same or from any of its shareholders' or duly appointed agents, shares of the company or other body corporate, whether by conversion of the bond or warrant or otherwise, on the basis of the price agreed upon when the same was issued.

If the Central Government is satisfied that in the interest of trade and commerce or the economic development of the country, it is necessary or expedient so to do, it may, by notification in the Official Gazette, specify any class of contracts as contracts to which this Act or any provision contained therein shall not apply, and also the conditions, limitations or restrictions, if any, subject to which it shall not so apply.

DEFINITIONS

Section 2 of this Act contains definitions of various terms used in the Act. Some of the important definitions are given below:

Securities

Securities include –

- (i) shares, scrips, stocks, bonds, debentures, debenture stock or other marketable securities of a like nature in or of any incorporated company or body corporate;
- (ii) derivative;
- (iii) units or any other instrument issued by any collective investment scheme to the Investors in such schemes;
- (iv) security receipt as defined in clause (zg) of Section 2 of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002;
- (v) units or any other such instrument issued to the investors under any mutual fund scheme;

Explanation : “securities” shall not include any unit linked insurance policy or scripts or any such instrument or unit, by whatever name called, which provides a combined benefit risk on the life of the persons and investment by such person and issued by an insurer referred to in clause (9) of section 2 of the Insurance Act, 1938.

- (vi) any certificate or instrument (by whatever name called) issued to an investor by any issuer being a special purpose distinct entity which possess any debt or receivable, including mortgage debt, assigned to such entity, and acknowledging beneficial interest of such investor in such debt or receivable, including mortgage debt, as the case may be;
- (vii) government securities;
- (viii) such other instruments as may be declared by the Central Government to be securities; and
- (ix) rights or interests in securities.

Spot delivery contract

Spot delivery contract means a contract which provides for –

- (a) actual delivery of securities and the payment of a price therefore either on the same day as the date of the contract or on the next day, the actual period taken for the dispatch of the securities or the remittance of money therefore through the post being excluded from the computation of the period aforesaid if the parties to the contract do not reside in the same town or locality;
- (b) transfer of the securities by the depository from the account of a beneficial owner to the account of another beneficial owner when such securities are dealt with by a depository.

Stock Exchange

Stock Exchange means –

- (a) any body of individuals, whether incorporated or not, constituted before corporatisation and demutualisation under Sections 4A and 4B, or
- (b) a body corporate incorporated under the Companies Act, 2013 whether under a scheme of corporatisation and demutualisation or otherwise, for the purpose of assisting, regulating or controlling the business of buying, selling or dealing in securities.

Recognised Stock Exchange

Recognised Stock Exchange means a stock exchange which is for the time being recognised by the Central Government.

Government security

Government security means a security created and issued whether before or after the commencement of this Act, by the Central Government or a State Government for the purpose of raising a public loan and having one of the forms specified in clause (2) of section 2 of the Public Debt Act, 1944.

Derivative

A derivative includes –

- (a) a security derived from a debt instrument, share, loan, whether secured or unsecured, risk instrument or contract for differences or any other form of security and;
- (b) a contract which derives its value from the prices or index of prices, of underlying securities.
- (c) Commodity derivatives; and
- (d) such other instruments as may be declared by the Central Government to be derivatives.

Non-transferable specific delivery contract

“Non-transferable specific delivery contract” means a specific delivery contract, the rights or liabilities under which or under any delivery order, railway receipt, bill of lading, warehouse receipt or any other documents of title relating thereto are not transferable.

Ready Delivery Contract

“Ready Delivery Contract” means a contract which provides for the delivery of goods and the payment of a price therefore, either immediately, or within such period not exceeding eleven days after the date of the contract and subject to such conditions as the Central Government may, by notification in the Official Gazette, specify in respect of any goods, the period under such contract not being capable of extension by the mutual consent of the parties thereto or otherwise.

However, where any such contract is performed either wholly or in part:

- (I) by realisation of any sum of money being the difference between the contract rate and the settlement rate or clearing rate or the rate of any offsetting contract; or
- (II) by any other means whatsoever, and as a result of which the actual tendering of the goods covered by the contract or payment of the full price therefore is dispensed with, then such contract shall not be deemed to be a ready delivery contract.

Transferable specific delivery contract

“Transferable specific delivery contract” means a specific delivery contract which is not a non-transferable specific delivery contract and which is subject to such conditions relating to its transferability as the Central Government may by notification in the Official Gazette specify in this behalf.

RECOGNITION OF STOCK EXCHANGES

Section 3 lays down that any stock exchange, desirous of being recognized for the purposes of this Act may make an application in the prescribed manner to the Central Government.

Every application shall contain such particulars as may be prescribed, and shall be accompanied by a copy of the bye-laws of the stock exchange for the regulation and control of contracts and also a copy of the rules relating in general to the constitution of the stock exchange and in particular to –

- (a) the governing body of such stock exchange, its constitution and powers of management and the manner in which its business is to be transacted;
- (b) the powers and duties of the office bearers of the stock exchange;
- (c) the admission into the stock exchange of various classes of members, the qualifications, for membership, and the exclusion, suspension, expulsion and re-admission of members therefrom or thereinto;
- (d) the procedure for the registration of partnerships as members of the stock exchange in cases where the rules provide for such membership; and the nomination and appointment of authorized representatives and clerks.

Section 4 lays down that if the Central Government is satisfied (powers are exercisable by SEBI also) after making such inquiry as may be necessary in this behalf and after obtaining such further information, if any, as it may require;

- (a) that the rules and bye-laws of a stock exchange applying for registration are in conformity with such conditions as may be prescribed with a view to ensure fair dealing and to protect investors;
- (b) that the stock exchange is willing to comply with any other conditions (including conditions as to the number of members) which the Central Government, after consultation with the governing body of the stock exchange and having regard to the area served by the stock exchange and its standing and the nature of the securities dealt with by it, may impose for the purpose of carrying out the objects of this Act; and
- (c) that it would be in the interest of the trade and also in the public interest to grant recognition to the stock exchange;

It may grant recognition to the stock exchange subject to the conditions imposed upon it as aforesaid and in such form as may be prescribed.

The conditions which the Central Government can prescribe for the grant of recognition to the stock exchanges may include, among other matters, conditions relating to –

- (i) the qualifications for membership of stock exchanges;
- (ii) the manner in which contracts shall be entered into and enforced as between members;
- (iii) the representation of the Central Government on each of the stock exchanges by such number of persons not exceeding three as the Central Government may nominate in this behalf; and
- (iv) the maintenance of accounts of members and their audit by chartered accountants whenever such audit is required by the Central Government.

Every grant of recognition to a stock exchange under this section shall be published in the Gazette of India and also in the Official Gazette of the State in which the principal office of the stock exchange is situated, and such recognition shall have effect as from the date of its publication in the Gazette of India.

No application for the grant of recognition shall be refused except after giving an opportunity to the stock exchange concerned to be heard in the matter; and the reasons for such refusal shall be communicated to the stock exchange in writing.

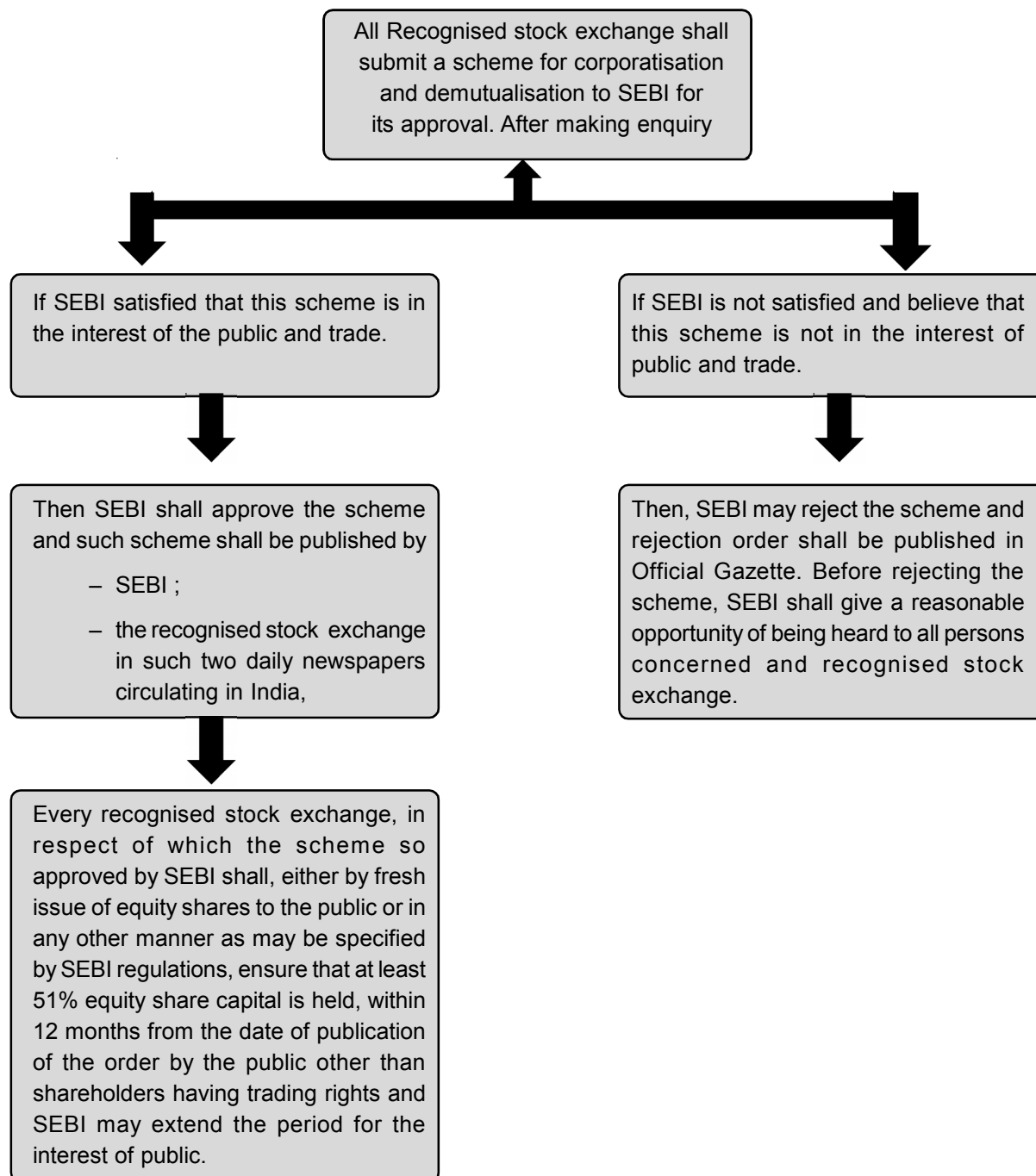
No rules of a recognised stock exchange relating to any of the matter specified above as conditions for grant of recognition by the Central Government shall be amended except with the approval of the Central Government.

CORPORATISATION AND DEMUTUALISATION OF STOCK EXCHANGES

Section 4A of the Act provides that on and from the appointed date, all recognized stock exchanges (if not corporatized and demutualised before the appointed date) shall be corporatized and demutualised in accordance with the provisions contained in Section 4B.

Further SEBI may, if it is satisfied that any recognized stock exchange was prevented by sufficient cause from being corporatized and demutualised on or after the appointed date, specify another appointed date in respect of that recognized stock exchange and such recognized stock exchange may continue as such before such appointed date.

PROCEDURE FOR CORPORATISATION AND DEMUTUALISATION



Note :- 1. SEBI may, while approving the scheme by an order in writing, restrict—

- (a) the voting rights of the shareholders who are also stock brokers of the recognised stock exchange;
- (b) the right of shareholders or a stock broker of the recognised stock exchange to appoint the representatives on the governing board of the stock exchange;
- (c) the maximum number of representatives of the stock brokers of the recognised stock exchange to be appointed on the governing board of the recognised stock exchange, which shall not exceed one-fourth of the total strength of the governing board.

2. No scheme shall be approved by SEBI if the issue of shares for a lawful consideration or provision of trading rights in lieu of membership card of the members of a recognised stock exchange or payment of dividends to members have been proposed out of any reserves or assets of that stock exchange.

3. The scheme so approved shall be binding on all persons and authorities including all members, creditors, depositors and employees of the recognised stock exchange and on all persons having any contract, right, power, obligation or liability with, against over to or in connection with, the recognised stock exchange or its members.

WITHDRAWAL OF RECOGNITION

Section 5 lays down that if the Central Government is of opinion that the recognition granted to a stock exchange should in the interest of the trade or in the public interest, be withdrawn, the Central Government may serve on the governing body of the stock exchange a written notice that the Central Government is considering the withdrawal of the recognition for the reasons stated in the notice and after giving an opportunity to the governing body to be heard in the matter, the Central Government may withdraw, by notification in the Official Gazette, the recognition granted to the stock exchange;

However, the withdrawal shall not affect the validity of any contract entered into or made before the date of the notification, and the Central Government may, after consultation with the stock exchange, make such provision as it deems fit in the notification of withdrawal or in any subsequent notification similarly published for the due performance of any contracts outstanding on that date.

Where the recognized stock exchange has not been corporatized or demutualised or it fails to submit the scheme within the specified time therefore or the scheme has been rejected by the SEBI, the recognition granted to such stock exchange, shall, notwithstanding anything to the contrary contained in this Act, stand withdrawn and the Central Government shall publish, by notification in the Official Gazette, such withdrawal of recognition.

However, such withdrawal shall not affect the validity of any contract entered into or made before the date of the notification, and SEBI may, after consultation with the stock exchange, make such provisions as it deems fit in the order rejecting the scheme published in the Official Gazette under sub-Section (5) of Section 4B.

It is to be noted that the powers under Section 4 (3), 4(5) and Section 5 have been delegated concurrently to SEBI also. Hence, SEBI may exercise these powers.

POWER OF CENTRAL GOVERNMENT TO CALL FOR PERIODICAL RETURNS AND MAKE DIRECT ENQUIRIES

Section 6 enjoins that every recognised stock exchange shall furnish to SEBI, such periodical returns relating to its affairs as may be prescribed. Every such stock exchange and every member thereof shall maintain and preserve for such periods not exceeding five years such books of accounts, and other documents as the Central Government, after consultation with the stock exchange concerned, may prescribe in the interest of the trade or in the public interest, and such books of account, and other documents shall be subject to inspection to all reasonable times by SEBI.

If SEBI is satisfied that it is in the interest of the trade or in public interest so to do, may by order in writing –

- (a) call upon a recognised stock exchange or any member thereof to furnish in writing such information or explanation relating to the affairs of the stock exchange or of the member in relation to the stock exchange as SEBI may require; or
- (b) appoint one or more persons to make an inquiry in the prescribed manner in relation to the affairs of the governing body of a stock exchange or the affairs of any of the members of the stock exchange in relation to the stock exchange and submit a report of the result of such inquiry to the SEBI within such

time as may be specified in the order or, in the case of an inquiry in relation to the affairs of any of the members of a stock exchange, direct the governing body to make the inquiry and submit its report to SEBI.

Where an inquiry in relation to the affairs of a recognised stock exchange or the affairs of any of its members in relation to the stock exchange has been undertaken –

- (a) every director, manager, secretary or other officer of such stock exchange;
- (b) every member of such stock exchange;
- (c) if the member of the stock exchange is a firm, every partner, manager, secretary or other officer of the firm; and
- (d) every other person or body of persons who has had dealings in the course of business with any of the persons mentioned in clauses (a), (b) and (c) whether directly or indirectly; shall be bound to produce before the authority making the inquiry all such books of account, and other documents in his custody or power relating to or having a bearing on the subject-matter of such inquiry and also to furnish the authorities within such time as may be specified with any such statement or information relating thereto as may be required of him.

Every stock exchange shall furnish to the Central Government and to SEBI a copy of its annual report which shall contain such particulars as may be prescribed by Central Government/SEBI.

POWER OF RECOGNISED STOCK EXCHANGE TO MAKE RULES RESTRICTING VOTING RIGHTS ETC.

Section 7A of the Act stipulates that a recognised stock exchange may make rules or amend any rules made by it to provide for all or any of the following matters, namely –

- (a) the restriction of voting rights to members only in respect of any matter placed before the stock exchange at any meeting;
- (b) the regulation of voting rights in respect of any matter placed before the stock exchange at any meeting so that each member may be entitled to have one vote only, irrespective of his share of the paid-up equity capital of the stock exchange;
- (c) the restriction on the right of a member to appoint another person as his proxy to attend and vote at a meeting of the stock exchange; and
- (d) such incidental, consequential and supplementary matters as may be necessary to give effect to any of the matters specified in clauses (a) (b) and (c).

No rules of a recognised stock exchange made or amended in relation to any matter referred in the above paragraph shall have effect until they have been approved by the Central Government and published by that Government in the Official Gazette and, in approving the rules so made or amended, the Central Government may make such modifications therein as it thinks fit, and on such publication, the rules as approved by the Central Government shall be deemed to have been validly made, notwithstanding anything to the contrary contained in the Companies Act, 2013. The powers have been delegated concurrently to SEBI also in this regard.

POWER OF CENTRAL GOVERNMENT TO DIRECT RULES OR MAKE RULES

Section 8 deals with the power of Central Government to make rules or direct rules to be made in respect of recognised stock exchange. Where after consultation with the governing bodies of stock exchanges generally or with the governing body of any stock exchange in particular, the Central Government is of opinion that it is necessary or expedient so to do, it may, by order in writing together with a statement of the reasons therefor, direct the recognised stock exchanges generally or any recognised stock exchange in particular, as the case

may be, to make any rules or to amend any rules already made in respect of all or any of the matters or to amend any rules already made in respect of all or any of the matters as specified, within a period of two months from the date of the order.

If any recognised stock exchange fails or neglects to comply with any order, within the period specified therein, the Central Government may make the rules for, or amend the rules made by, the recognised stock exchange, either in the form proposed in the order or with such modifications thereof as may be agreed to between the stock exchange and the Central Government.

Where in pursuance of this section any rules have been made or amended, the rules so made or amended shall be published in the Gazette of India and also in the Official Gazette or Gazettes of the State or States in which the principal office or offices of the recognised stock exchange or exchanges is or are situate, and, on the publication thereof in the Gazette of India, the rules so made or amended shall, notwithstanding anything to the contrary contained in the Companies Act, 2013 or in any other law for the time being in force, have effect as if they had been made or amended by the recognised stock exchange or stock exchanges, as the case may be.

Powers have been delegated concurrently to SEBI also.

CLEARING CORPORATION

Section 8A(1) provides that a recognised stock exchange may, with the prior approval of SEBI, transfer the duties and functions of a clearing house to a clearing corporation, being a company incorporated under the Companies Act, 2013, for the purpose of –

- (a) the periodical settlement of contracts and differences thereunder;
- (b) the delivery of, and payment for, securities;
- (c) any other matter incidental to, or connected with, such transfer.

Sub-section (2) provides that every clearing corporation shall, for the purpose of transfer of the duties and functions of a clearing house to a clearing corporation referred to in sub-section (1), make bye-laws and submit the same to the SEBI for its approval.

Sub-section (3) provides that SEBI may, on being satisfied that it is in the interest of the trade and also in the public interest to transfer the duties and functions of a clearing house to a clearing corporation, grant approval to the bye-laws submitted to it and approve transfer of the duties and functions of a clearing house to a clearing corporation.

POWER OF RECOGNISED STOCK EXCHANGES TO MAKE BYE-LAWS

According to Section 9, any recognised stock exchange may, subject to the previous approval of SEBI, make bye-laws for the regulation and control of contracts. In particular, and without prejudice to the generality of the foregoing power, such bye-laws may provide for:

- (a) the opening and closing of markets and the regulation of the hours of trade;
- (b) a clearing house for the periodical settlement of contracts and differences thereunder, the delivery of and payment for securities, the passing on of delivery orders and the regulation and maintenance of such clearing house;
- (c) the submission to SEBI by the clearing house as soon as may be after each periodical settlement of all or any of the following particulars as SEBI may, from time to time, require, namely:
 - (i) the total number of each category of security carried over from one settlement period to another;
 - (ii) the total number of each category of security, contracts which have been squared up during the course of each settlement period;

- (iii) the total number of each category of security actually delivered at each clearing;
- (d) the publication by the clearing house of all or any of the particulars submitted to SEBI subject to the directions, if any, issued by SEBI in this behalf;
- (e) the regulation or prohibition of blank transfers;
- (f) the number and classes of contracts in respect of which settlements shall be made or differences paid through the clearing house;
- (g) the regulation, or prohibition of *budlas* or carry-over facilities;
- (h) the fixing, altering or postponing of days for settlements;
- (i) the determination and declaration of market rates, including the opening, closing, highest and lowest rates for securities;
- (j) the terms, conditions and incidents of contracts, including the prescription of margin requirements, if any, and conditions relating thereto, and the forms of contracts in writing;
- (k) the regulation of the entering into making, performance, rescission and termination, of contracts, including contracts between members or between a member and his constituent or between a member and a person who is not a member, and the consequences of default or insolvency on the part of a seller or buyer or intermediary, the consequences of a breach or omission by a seller or buyer, and the responsibility of members who are not parties to such contracts;
- (l) the regulation of *taravani* business including the placing of limitations thereon;
- (m) the listing of securities on the stock exchange, the inclusion of any security for the purpose of dealings and the suspension or withdrawal of any such securities, and the suspension or prohibition of trading in any specified securities;
- (n) the method and procedure for the settlement of claims or disputes, including settlement by arbitration;
- (o) the levy and recovery of fees, fines and penalties;
- (p) the regulation of the course of business between parties to contracts in any capacity;
- (q) the fixing of a scale of brokerage and other charges;
- (r) the making, comparing, settling and closing of bargains;
- (s) the emergencies in trade which may arise, whether as a result of pool or syndicated operations or concerning or otherwise, and the exercise of powers in such emergencies including the power to fix maximum and minimum prices for securities;
- (t) the regulation of dealings by members for their own account;
- (u) the separation of the functions of jobbers and brokers;
- (v) the limitations on the volume of trade done by any individual member in exceptional circumstances;
- (w) the obligation of members to supply such information or explanation and to produce such documents relating to the business as the governing body may require.

PUNISHMENTS FOR CONTRAVENTIONS

The bye-laws made under Section 9 may;

- (a) specify the bye-laws, the contravention of which shall make a contract entered into otherwise than in accordance with the bye-laws void under sub-section (1) of section 14 (which specifies contract in notified areas to be void).

- (b) provide that the contravention of any of the bye-laws shall render the member concerned liable to one or more of the following punishments, namely;
 - (i) fine,
 - (ii) expulsion from membership,
 - (iii) suspension from membership for a specified period,
 - (iv) any other penalty of a like nature not involving the payment of money.

Any bye-laws made under this section shall be subject to such conditions in regard to previous publication as may be prescribed, and when approved by SEBI, shall be published in the Gazette of India and also in the Official Gazette of the State in which the principal office of the recognised stock exchange is situated, and shall have effect as from the date of its publication in the Gazette of India.

However, if SEBI is satisfied in any case that in the interest of the trade or in the public interest any bye-laws should be made immediately, it may, by order in writing specify the reasons therefor, dispense with the condition of previous publication.

POWER OF SEBI TO MAKE OR AMEND BYE-LAWS OF RECOGNISED STOCK EXCHANGES

SEBI may, either on a request in writing received by it in this behalf from the governing body of a recognised stock exchange or on its own motion, if it is satisfied after consultation with the governing body of the stock exchange that it is necessary or expedient so to do and after recording its reasons for so doing, make bye-laws, for all or any of the matters specified in section 9 or amend any bye-laws made by such stock exchange under that section.

Where in pursuance of this section, any bye-laws have been made or amended, the bye-laws so made or amended shall be published in the Gazette of India and also in the Official Gazette of the State in which the principal office of the recognised stock exchange is situated, and on the publication thereof in the Gazette of India, the bye-laws so made or amended shall have effect as if they had been made or amended by the recognised stock exchange concerned.

Where the governing body of a recognised stock exchange objects to any bye-laws made or amended by SEBI on its own motion, it may, within two months of the publication thereof in the Gazette of India apply to SEBI for revision thereof and SEBI may, after giving an opportunity to the governing body of the stock exchange to be heard in the matter, revise the bye-laws so made or amended, and where any bye-laws so made or amended are revised as a result of any action taken under this sub-section, the bye-laws so revised shall be published and shall become effective as provided in sub-section (2) of Section 10.

The making or the amendment or revision of any bye-laws shall in all cases be subject to the condition of previous publication.

However, if SEBI is satisfied in any case that in the interest of the trade or in the public interest any bye-laws should be made, amended or revised immediately, it may, by order in writing specifying the reasons therefor, dispense with the condition of previous publication.

POWER OF CENTRAL GOVERNMENT TO SUPERSEDE COMPANIES OF STOCK EXCHANGES OR SUSPEND BUSINESS THEREOF

Without prejudice to any other powers vested in the Central Government under this Act, where the Central Government is of opinion that the governing body of any recognised stock exchange should be superseded, then, notwithstanding anything contained in any other law for the time being in force, the Central Government may serve on the governing body a written notice that the Central Government is considering the supersession of the governing body for the reasons specified in the notice and after giving an opportunity to the governing body to be heard in the matter, it may, by notification in the Official Gazette, declare the governing body of such

stock exchange to be superseded, and may appoint any person or persons to exercise and perform all the powers and duties of the governing body, and, where more persons than one are appointed, may appoint one of such persons to be the chairman and another to be the vice-chairman thereof.

On the publication of a notification in the Official Gazette, the following consequences shall ensure, namely –

- (a) the members of the governing body which has been superseded shall, as from the date of the notification of super session, cease to hold office as such members;
- (b) the person or persons appointed may exercise and perform all the powers and duties of the governing body which has been superseded;
- (c) all such property of the recognised stock exchange as the person or persons appointed may, by order in writing, specify in this behalf as being necessary for the purpose of enabling him or them to carry on the business of the stock exchange, shall vest in such person or persons.

Notwithstanding anything to the contrary contained in any law or the rules or bye-laws of the recognised stock exchange the governing body of which is superseded, the person or persons appointed under that sub-section shall hold office for such period as may be specified in the notification published under that sub-section and, the Central Government may from time to time, by notification, vary such period.

The Central Government, may at any time before the determination of the period of office of any person or persons appointed under this section call upon the recognised stock exchange to reconstitute the governing body in accordance with its rules and on such re-constitution all the property of the recognised stock exchange which has been vested in, or was in the possession of, the person or persons appointed, shall vest or re-vest, as the case may be, in the governing body so re-constituted;

However, until a governing body is so re-constituted, the person or persons appointed, shall continue to exercise and perform their powers and duties.

Power to Suspend Business of Recognised Stock Exchange

If in the opinion of the Central Government an emergency, has arisen, for the purpose of meeting the emergency, the Central Government considers it expedient so to do, it may, by notification in the Official Gazette, for reasons to be set out therein, direct a recognised stock exchange to suspend such of its business for such period not exceeding seven days and subject to such conditions as may be specified in the notification, and if, in the opinion of the Central Government, the interest of the trade or the public interest requires that the period should be extended, may, by like notification extend the said period from time to time;

However, where the period of suspension is to be extended beyond the first period, no notification extending the period of suspension shall be issued unless the governing body of the recognised stock exchange has been given an opportunity of being heard in the matter.

Power to Issue Directions

Section 12A provides that if, after making or causing to be made an inquiry, SEBI is satisfied that it is necessary –

- (a) in the interest of investors, or orderly development of securities market; or
- (b) to prevent the affairs of any recognised stock exchange, or, clearing corporation, or such other agency or person, providing trading or clearing or settlement facility in respect of securities, being conducted in a manner detrimental to the interests of investors or securities market; or
- (c) to secure the proper management of any such stock exchange or clearing corporation or agency or person, referred to in clause (b), it may issue such directions –
 - (i) to any stock exchange or clearing corporation or agency or person referred to in clause (b) or any person or class of persons associated with the securities market; or

- (ii) to any company whose securities are listed or proposed to be listed in a recognised stock exchange, as may be appropriate in the interests of investors in securities and the securities market.

Explanation : The power to issue directions under this section shall include and always be deemed to have been included the power to direct any person, who made profit or averted loss by indulging in any transaction or activity in contravention of the provisions of this Act or regulations made thereunder, to disgorge an amount equivalent to the wrongful gain made or loss averted by such contraventions.

CONTRACTS IN SECURITIES

If the Central Government is satisfied, having regard to the nature or the volume of transactions in securities in any State or States or area, that it is necessary so to do, it may, by notification in the Official Gazette, declare that section 13 to apply to such State or States or area, and thereupon every contract in such State or States or area which is entered into after date of the notification otherwise than between members of a recognised stock exchange or recognised stock exchanges in such State or States or area or through or with such member shall be illegal.

However, any contract entered into between members of two or more recognised stock exchanges in such State or States or area, shall –

- (i) be subject to such terms and conditions as may be stipulated by the respective stock exchanges with prior approval of SEBI;
- (ii) require prior permission from the respective stock exchanges if so stipulated by the stock exchanges with prior approval of SEBI.

Additional Trading Floor

A stock exchange may establish additional trading floor with the prior approval of SEBI in accordance with the terms and conditions stipulated by SEBI.

Additional trading floor means a trading ring or trading facility offered by a recognised stock exchange outside its area of operating to enable the investors to buy and sell securities through such trading floor under the regulatory framework of that stock exchange.

Contract in certain areas to be void

Any contract entered into in any State or area specified in the notification under section 13 which is in contravention of any of the bye-laws specified in that behalf under clause(a) of sub-section (3) of section 9 shall be void:

- (i) as respects the rights of any member of the recognised stock exchange who has entered into such contract in contravention of any such bye-laws, and also
- (ii) as respects the rights of any other person who has knowingly participated in the transaction entailing such contravention.

Nothing in sub-section (1) shall be construed to affect the right of any person other than a member of the recognised stock exchange to enforce any such contract or to recover any sum under or in respect of such contract if such person had no knowledge that the transaction was in contravention of any of the bye-laws specified in clause (a) of sub-section (3) of section 9.

Members may not act as principals in certain circumstances.

No member of a recognised stock exchange shall in respect of any securities enter into any contract as a principal with any person other than a member of a recognised stock exchange, unless he has secured the consent or authority of such person and discloses in the note, memorandum or agreement of sale or purchase that he is acting as a principal.

However, where the member has secured the consent or authority of such person otherwise than in writing he shall secure written confirmation by such person or such consent or authority within 3 days from the date of contract.

Further that no such written consent or authority of such person shall be necessary for closing out any outstanding contract entered into by such person in accordance with the bye-laws, if the member discloses in the note, memorandum or agreement of sale or purchase in respect of such closing out that he is acting as a principal.

Power to Prohibit Contracts in Certain Cases

If the Central Government is of opinion that it is necessary to prevent undesirable speculation in specified securities in any State or area, it may, by notification in the Official Gazette, declare that no person in the State or area specified in the notification shall, save with the permission of the Central Government, enter into any contract for the sale or purchase of any security specified in the notification except to the extent and in the manner, if any, specified therein.

All contracts in contravention of the provisions of sub-section (1) entered into after the date of the notification issued thereunder shall be illegal.

Licensing of dealers in certain areas

Subject to the provision of sub-section (3) and to the other provisions contained in this Act, no person shall carry on or purport to carry on, whether on his own behalf or on behalf of any other person, the business of dealing in securities in any State or area to which section 13 has not been declared to apply and to which the Central Government may, by notification in the Official Gazette, declare this section to apply, except under the authority of a license granted by SEBI in this behalf.

No notification under sub-section (1) shall be issued with respect to any State or area unless the Central Government is satisfied, having regard to the manner in which securities are being dealt with in such State or area, that it is desirable or expedient in the interest of the trade or in the public interest that such dealings should be regulated by a system of licensing.

The restrictions imposed by sub-section (1) in relation to dealings in securities shall not apply to the doing of anything by or on behalf of a member of any recognised stock exchange.

PUBLIC ISSUE AND LISTING OF SECURITIES

Section 17A provides for public issue and listing of securities.

Without prejudice to the provisions contained in this Act or any other law for the time being in force, no securities of the nature referred to in sub-clause (ie) of clause (h) of section 2 shall be offered to the public or listed on any recognized stock exchange unless the issuer fulfils such eligibility criteria and complies with such other requirements as may be specified by regulations made by SEBI.

Every issuer intending to offer the certificates or instruments referred therein to the public shall make an application, before issuing the offer document to the public, to one or more recognized stock exchanges for permission for such certificates or instruments to be listed on the stock exchange or each such stock exchange.

Where the permission applied for listing has not been granted or refused by the recognized stock exchanges or any of them, the issuer shall forthwith repay all moneys, if any, received from applicants in pursuance of the offer document, and if any such money is not repaid within eight days after the issuer becomes liable to repay it, the issuer and every director or trustee thereof, as the case may be, who is in default shall, on and from the expiry of the eighth day, be jointly and severally liable to repay that money with interest at the rate of fifteen per cent per annum.

In reckoning the eighth day after another day, any intervening day which is a public holiday under the Negotiable Instruments Act, 1881, shall be disregarded, and if the eighth day (as so reckoned) is itself such a public holiday, there shall for the said purposes be substituted the first day thereafter which is not a holiday.

All the provisions of this Act relating to listing of securities of a public company on a recognized stock exchange shall, *mutates mutandis*, apply to the listing of the securities of the nature referred to in sub-clause (ie) of clause (h) of section 2 by the issuer, being a special purpose distinct entity.

EXCLUSION OF SPOT DELIVERY CONTRACTS

If the Central Government is of opinion that in the interest of the trade or in the public interest, it is expedient to regulate and control the business of dealing in spot delivery contracts also in any State or area (whether section 13 has been declared to apply to that State or area or not), it may, by notification in the Official Gazette, declare that the provisions of section 17 shall also apply to such State or area in respect of spot delivery contracts generally or in respect of spot delivery contract for the sale or purchase of such securities as may be specified in the notification, and may also specify the manner in which, and the extent to which, the provisions of that section shall so apply.

CONTRACTS IN DERIVATIVES

Notwithstanding anything contained in any other law for the time being in force, contracts in derivative shall be legal and valid if such contracts are –

- (a) traded on a recognised stock exchange;
- (b) settled on the clearing house of the recognised stock exchange, or
- (c) between such parties and on such terms as the Central Government may, by notification in the official Gazette, specify, in accordance with the rules and bye-laws of such stock exchange.

CONDITIONS FOR LISTING

Section 21 of the Act provides that where securities are listed on the application of any person in any recognised stock exchange, such person shall comply with the conditions of the listing agreement with that stock exchange.

DELISTING OF SECURITIES

Section 21A provides that a recognised stock exchange may delist the securities, after recording the reasons therefor, from any recognised stock exchange on any of the ground or grounds as may be prescribed under this Act.

The securities of a company shall not be delisted unless the company concerned has been given a reasonable opportunity of being heard.

A listed company or an aggrieved investor may file an appeal before the Securities Appellate Tribunal (SAT) against the decision of the recognised stock exchange delisting the securities within fifteen days from the date of the decision of the recognized stock exchange delisting the securities and the provisions of Sections 22B to 22E of this Act, shall apply, as far as may be, to such appeals.

The Securities Appellate Tribunal may, if it is satisfied that the company was prevented by sufficient cause from filing the appeal within the said period, allow it to be filed within a further period not exceeding one month.

RIGHT OF APPEAL TO SAT AGAINST REFUSAL TO LIST SECURITIES OF PUBLIC COMPANIES BY STOCK EXCHANGES

Where a recognised stock exchange, acting in pursuance of any power given to it by its bye-laws, refuses to list the securities of any company, the company shall be entitled to be furnished with reasons for such refusal, and may, –

- (a) within fifteen days from the date on which the reasons for such refusal are furnished to it, or
- (b) where the stock exchange has omitted or failed to dispose of, within the time specified in sub-section (1A) of section 40 of the Companies Act, 2013, the application for permission for the shares or debentures to be dealt with on the stock exchange, within fifteen days from the date of expiry of the specified time or within such further period, not exceeding one month, as the Securities Appellate Tribunal may, on sufficient cause being shown, allow appeal to the Securities Appellate Tribunal having jurisdiction in the matter against such refusal, omission or failure, as the case may be, and thereupon the Securities Appellate Tribunal may, after giving the stock exchange, an opportunity of being heard, –
 - (i) vary or set aside the decision of the stock exchange; or
 - (ii) where the stock exchange has omitted or failed to dispose of the application within the specified time, grant or refuse the permission, and where the Securities Appellate Tribunal sets aside the decision of the recognised stock exchange or grants the permission, the stock exchange shall act in conformity with the orders of the Securities Appellate Tribunal.

Every appeal under sub-section (1) shall be in such form and be accompanied by such fee as may be prescribed. The Securities Appellate Tribunal shall send a copy of every order made by it to SEBI and parties to the appeal.

The appeal filed before the Securities Appellate Tribunal under sub-section (1) shall be dealt with by it as expeditiously as possible and endeavour shall be made by it to dispose of the appeal finally within six months from the date of receipt of the appeal.

PROCEDURE AND POWERS OF SAT

The Securities Appellate Tribunal shall not be bound by the procedure laid down by the Code of Civil Procedure, 1908, but shall be guided by the principles of natural justice and, subject to the other provisions of this Act and of any rules, the Securities Appellate Tribunal shall have powers to regulate their own procedure including the places at which they shall have their sittings.

The Securities Appellate Tribunal shall have, for the purpose of discharging their functions under this Act, the same powers as are vested in a civil court under the Code of Civil Procedure, 1908, while trying a suit, in respect of the following matters, namely –

- (a) summoning and enforcing the attendance of any person and examining him on oath;
- (b) requiring the discovery and production of documents;
- (c) receiving evidence on affidavits;
- (d) issuing commissions for the examination of witnesses or documents;
- (e) reviewing its decisions;
- (f) dismissing an application for default or deciding it *ex parte*;
- (g) setting aside any order of dismissal of any application for default or any order passed by it *ex parte*; and
- (h) any other matter which may be prescribed.

Every proceeding before the Securities Appellate Tribunal shall be deemed to be a judicial proceeding within the meaning of sections 193 and 228, and for the purposes of section 196 of the Indian Penal Code, 1860 and the Securities Appellate Tribunal shall be deemed to be a civil court for all the purposes of section 195 and Chapter XXVI of the Code of Criminal Procedure, 1973.

RIGHT TO LEGAL REPRESENTATION

The appellant may either appear in person or authorise one or more chartered accountants or company secretary or cost accountant or legal practitioners or any of its officers to present his or its case before the SAT.

APPEAL TO SUPREME COURT

Any person aggrieved by any decision or order of the Securities Appellate Tribunal may file an appeal to the Supreme Court within sixty days from the date of communication of the decision or order of the Securities Appellate Tribunal to him on any question of fact or law arising out of such order;

However, the Supreme Court may, if it is satisfied that the appellant was prevented by sufficient cause from filing the appeal within the said period, allow it to be filed within a further period not exceeding sixty days.

PENALTIES AND PROCEDURES

The Act prescribes various penalties against persons who might be found guilty of offences under section 23 the Act. These offences are listed below –

Any person who –

- (a) without reasonable excuse (the burden of proving which shall be on him) fails to comply with any requisition made under sub-section (4) of section 6; or
- (b) enters into any contract in contravention of any of the provisions contained in section 13 or section 16; or
- (c) contravenes the provisions contained in section 17 or section 17A or section 19; or
- (d) enters into any contract in derivative in contravention of section 18A or the rules made under section 30; or
- (e) owns or keeps a place other than that of a recognised stock exchange which is used for the purpose of entering into or performing any contracts in contravention of any of the provisions of this Act and knowingly permits such place to be used for such purposes; or
- (f) manages, controls, or assists in keeping any place other than that of a recognised stock exchange which is used for the purpose of entering into or performing any contracts in contravention of any of the provisions of this Act or at which contracts are recorded or adjusted or rights or liabilities arising out of contracts are adjusted, regulated or enforced in any manner whatsoever; or
- (g) not being a member of a recognised stock exchange or his agent authorised as such under the rules or bye-laws of such stock exchange or not being a dealer in securities licensed under section 17 willfully represents to or induces any person to believe that contracts can be entered into or performed under this Act through him; or
- (h) not being a member of a recognised stock exchange or his agent authorised as such under the rules or bye-laws of such stock exchange or not being a dealer in securities licensed under section 17, canvasses, advertises or touts in any manner either for himself or on behalf of any other person for any business connected with contracts in contravention of any of the provisions of this Act; or
- (i) joins, gathers or assists in gathering at any place other than the place of business specified in the bye-laws of a recognised stock exchange any person or persons for making bids or offers or for entering into or performing any contracts in contravention of any of the provisions of this Act,

shall, without prejudice to any award of penalty by the Adjudicating Officer under this Act, on conviction, be punishable with imprisonment for a term which may extend to ten years or with fine, which may extend to twenty-five crore rupees or with both.

Any person who enters into any contract in contravention of the provisions contained in section 15 or who fails to comply with the provisions of section 21 or section 21A or with the orders of or the Central Government under section 22 or with the orders of the Securities Appellate Tribunal shall, without prejudice to any award of penalty by the Adjudicating Officer under this Act, on conviction, be punishable with imprisonment for a term which may extend to ten years or with fine, which may extend to twenty five crore rupees, or with both.

PENALTIES

Penalty for failure to furnish information, return, etc.

- Any person, who is required under this Act or any rules made thereunder, fails to furnish any information, document, books, returns or report to a recognised stock exchange or fail to maintain books of account or records, as per the listing agreement or conditions, or bye-laws of a recognised stock exchange, shall be liable to a penalty which shall not be less than 1 lakh rupees and which may extend to one crore rupees for each day during which such failure continues.

Penalty for failure by any person to enter into an agreement with clients

- Any person, who is required under this Act or any bye-laws of a recognised stock exchange made thereunder, fails to enter into an agreement with his client, then he shall be liable to a penalty which shall not be less than 1 lakh rupees which may extend to one crore rupees for each day during which such failure continues.

Penalty for failure to redress investors' grievances

- Any stock broker or sub-broker or a company whose securities are listed or proposed to be listed in a recognised stock exchange, after having been called upon by SEBI or a recognised stock exchange in writing, to redress the grievances of the investors, fails to redress such grievances within the time, shall be liable to a penalty which shall not be less than 1 lakh rupees and which may extend to one crore rupees for each day during which such failure continues.

Penalty for failure to segregate securities or moneys of client or clients

- Any person, who is registered as a stock broker or sub-broker with SEBI, fails to segregate securities or moneys of the client or clients or uses the securities or moneys of a client or clients for self or for any other client, he shall be liable to a penalty which shall not be less than 1 lakh rupees and which may extend to one crore rupees.

Penalty for failure to comply with provision of listing conditions or delisting conditions or grounds

- If a company or any person managing collective investment scheme or mutual fund, fails to comply with the listing conditions or delisting conditions or grounds or commits a breach thereof, he shall be liable to a penalty which shall not be less than 5 lakh rupees and which may extend to 25 crore rupees.

Penalty for excess dematerialisation or delivery of unlisted securities

- If any company dematerialises securities more than the issued securities of a company or delivers in the stock exchanges the securities which are not listed in the recognised stock exchange or delivers securities where no trading permission has been given by the recognised stock exchange, he shall be liable to a penalty which shall not be less than 5 lakh rupees and which may extend to 25 crore rupees.

Penalty for failure to furnish periodical returns, etc.

- If a recognised stock exchange fails or neglects to furnish periodical returns to SEBI or fails or neglects to make or amend its rules or bye-laws as directed by SEBI or fails to comply with directions issued by SEBI, such recognised stock exchange shall be liable to a penalty which shall not be less than 5 lakh rupees and which may extend to 25 crore rupees.

Penalty for contravention where no separate penalty has been prescribed

- Where contravenues of any provision of this Act, the rules or articles or bye-laws or the regulations of the recognised stock exchange or directions issued by SEBI for which no separate penalty has been provided, shall be liable to a penalty which shall not be less than 1 lakh rupees and which may extend to 1 crore rupees.

POWER TO ADJUDICATE

Section 23-I deals with power to adjudicate by SEBI.

SEBI shall appoint any officer not below the rank of a Division Chief of SEBI to be an adjudicating officer for holding an inquiry in the prescribed manner after giving any person concerned a reasonable opportunity of being heard for the purpose of imposing any penalty.

While holding an inquiry, the adjudicating officer shall have power to summon and enforce the attendance of any person acquainted with the facts and circumstances of the case to give evidence or to produce any document, which in the opinion of the adjudicating officer, may be useful for or relevant to the subject-matter of the inquiry and if, on such inquiry, he is satisfied that the person has failed to comply with the provisions, he may impose such penalty as he thinks fit in accordance with the provisions of this Act.

SEBI may call for and examine the record of any proceedings under this section and if it considers that the order passed by the adjudicating officer is erroneous to the extent it is not in the interests of the securities market, it may, after making or causing to be made such inquiry as it deems necessary, pass an order enhancing the quantum of penalty, if the circumstances of the case so justify. However, no such order shall be passed unless the person concerned has been given an opportunity of being heard in the matter.

Further, nothing contained in this sub-section shall be applicable after an expiry of a period of three months from the date of the order passed by the adjudicating officer or disposal of the appeal under section 23L, whichever is earlier.

FACTORS TO BE TAKEN INTO ACCOUNT BY THE ADJUDICATING OFFICER

Section 23J provides for the factors to be taken into account by the adjudicating officer. While adjudging the quantum of penalty, the adjudicating officer shall have due regard to the following factors, namely –

- (a) the amount of disproportionate gain or unfair advantage, wherever quantifiable, made as a result of the default;
- (b) the amount of loss caused to an investor or group of investors as a result of the default;
- (c) the repetitive nature of the default.

Settlement of Administrative and Civil Proceedings

Section 23JA states that any person, against whom any proceedings have been initiated or may be initiated under section 12A or section 23-I, may file an application in writing to SEBI proposing for settlement of the proceedings initiated or to be initiated for the alleged defaults.

SEBI may, after taking into consideration the nature, gravity and impact of defaults, agree to the proposal for settlement, on payment of such sum by the defaulter or on such other terms as may be determined by SEBI in accordance with the regulations made under the SEBI Act, 1992.

For the purpose of settlement under this section, the procedure as specified by SEBI under the SEBI Act, 1992 shall apply.

No appeal shall lie under section 23L against any order passed by SEBI or adjudicating officer, as the case may be, under this section.

Recovery of Amounts

Section 23JB deals with recovery of amounts. If a person fails to pay the penalty imposed by the adjudicating officer or fails to comply with any direction of SEBI for refund of monies or fails to comply with a direction of disgorgement order issued under Section 12A or fails to pay any fees due to SEBI, the Recovery Officer may

draw up under his signature a statement in the specified form specifying the amount due from the person (such statement being hereafter in this Chapter referred to as certificate) and shall proceed to recover from such person the amount specified in the certificate by one or more of the following modes, namely:-

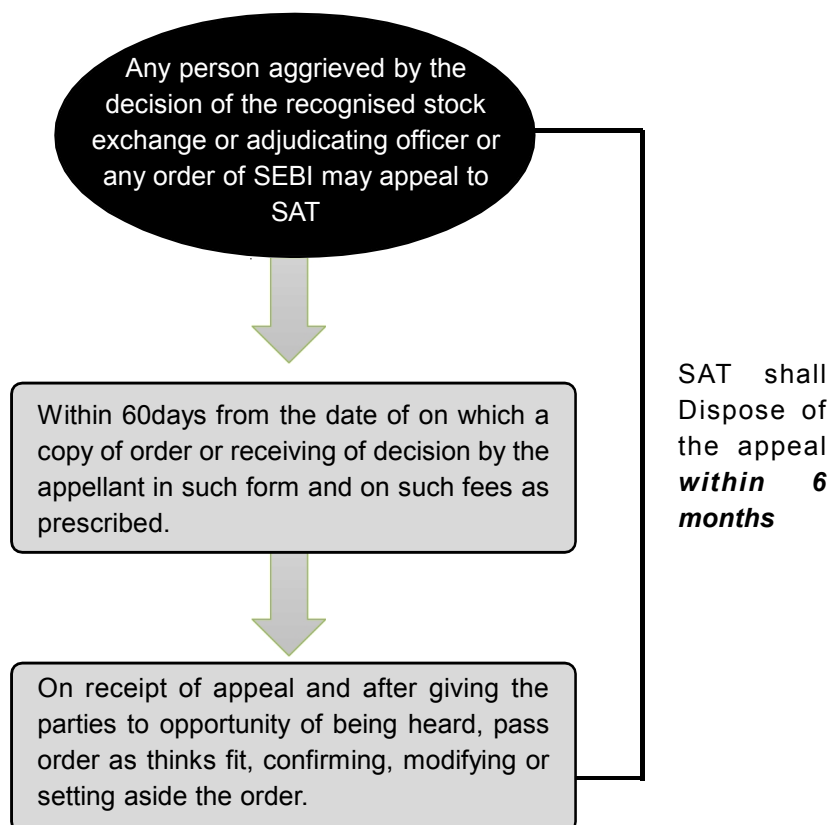
- (a) attachment and sale of the person's movable property;
- (b) attachment of the person's bank accounts;
- (c) attachment and sale of the person's immovable property;
- (d) arrest of the person and his detention in prison;
- (e) appointing a receiver for the management of the person's movable and immovable properties,

and for this purpose, the provisions of section 220 to 227, 228A, 229, 232, the Second and Third Schedules to the Income-tax Act, 1961 and the Income-tax (Certificate Proceedings) Rules, 1962, as in force from time to time, in so far as may be, apply with necessary modifications as if the said provisions and the rules thereunder were the provisions of this Act and referred to the amount due under this Act instead of to income-tax under the Income-tax Act, 1961.

CREDITING SUM REALISED BY WAY OF PENALTIES TO CONSOLIDATED FUND OF INDIA

All sums realised by way of penalties under this Act shall be credited to the Consolidated Fund of India.

APPEAL TO SECURITIES APPELLATE TRIBUNAL (SAT)



OFFENCES

(1) Without prejudice to any award of penalty by the adjudicating officer under this Act, if any person contravenes or attempts to contravene or abets the contravention of the provisions of this Act or of any rules or regulations or byelaws made thereunder, for which no punishment is provided elsewhere in this Act, he shall be punishable with imprisonment for a term which may extend to ten years, or with fine, which may extend to twenty-five crore rupees or with both.

(2) If any person fails to pay the penalty imposed by the adjudicating officer or fails to comply with any of his directions or orders, he shall be punishable with imprisonment for a term which shall not be less than one month but which may extend to ten years, or with fine, which may extend to twenty-five crore rupees, or with both. [Section 23M].

COMPOSITION OF CERTAIN OFFENCES

Notwithstanding anything contained in the Code of Criminal Procedure, 1973, any offence punishable under this Act, not being an offence punishable with imprisonment only, or with imprisonment and also with fine, may either before or after the institution of any proceeding, be compounded by a Securities Appellate Tribunal or a court before which such proceedings are pending. [Section 23N]

POWER TO GRANT IMMUNITY

Section 23-O deals with the power to grant immunity.

- (1) The Central Government may, on recommendation by SEBI, if the Central Government is satisfied, that any person, who is alleged to have violated any of the provisions of this Act or the rules or the regulations made thereunder, has made a full and true disclosure in respect of alleged violation, grant to such person, subject to such conditions as it may think fit to impose, immunity from prosecution for any offence under this Act, or the rules or the regulations made thereunder or also from the imposition of any penalty under this Act with respect to the alleged violation.

No such immunity shall be granted by the Central Government in cases where the proceedings for the prosecution for any such offence have been instituted before the date of receipt of application for grant of such immunity.

Further that the recommendation of the SEBI under this sub-section are not binding upon the Central Government.

- (2) An immunity granted to a person under sub-section (1) may, at any time, be withdrawn by the Central Government, if it is satisfied that such person had, in the course of the proceedings, not complied with the condition on which the immunity was granted or had given false evidence, and thereupon such person may be tried for the offence with respect to which the immunity was granted or for any other offence of which he appears to have been guilty in connection with the contravention and shall also become liable to the imposition of any penalty under this Act to which such person would have been liable, had not such immunity been granted.

OFFENCES BY COMPANIES

(1) Where an offence has been committed by a company, every person who, at the time when the offence was committed, was in charge of, and was responsible to, the company for the conduct of the business of the company, as well as the company, shall be deemed to be guilty of the offence, and shall be liable to be proceeded against and punished accordingly:

However, nothing contained in this sub-section shall render any such person liable to any punishment provided in this Act, if he proves that the offence was committed without his knowledge or that he exercised all due diligence to prevent the commission of such offence.

(2) Where an offence under this Act has been committed by a company and is proved that the offence has been committed with the consent or connivance of, or is attributable to any gross negligence on the part of any director,

manager, secretary or other officer of the company, such director, manager, secretary or other officer of the company shall also be deemed to be guilty of that offence and shall be liable to be proceeded against and punished accordingly.

(3) The provisions of this section shall be in addition to and not in derogation of, the provisions of section 22A.

CERTAIN OFFENCES TO BE COGNIZABLE

Notwithstanding anything contained in the Code of Criminal Procedure, 1898, any offence punishable under section 23 shall be deemed to be cognizable offence within the meaning of that Code.

COGNIZANCE OF OFFENCES BY COURTS

No court shall take cognizance of any offence punishable under this Act or any rules or regulations or bye-laws made thereunder, save on a complaint made by the Central Government or State Government or SEBI or a recognised stock exchange or by any person.

Establishment of Special Courts

Section 26A lays down the provisions for establishment of special courts by Central Govt. for the purpose of speedy trial.

(1) The Central Government may, for the purpose of providing speedy trial of offences under this Act, by notification, establish or designate as many Special Courts as may be necessary.

(2) A Special Court shall consist of a single judge who shall be appointed by the Central Government with the concurrence of the Chief Justice of the High Court within whose jurisdiction the judge to be appointed is working.

(3) A person shall not be qualified for appointment as a judge of a Special Court unless he is, immediately before such appointment, holding the office of a Sessions Judge or an Additional Sessions Judge, as the case may be.

Offences triable by Special Courts

Section 26B provides that notwithstanding anything contained in the Code of Criminal Procedure, 1973, all offences under this Act committed prior to the date of commencement of the Securities Laws (Amendment) Ordinance, 2014 or on or after the date of such commencement, shall be taken cognizance of and triable by the Special Court established for the area in which the offence is committed or where there are more Special Courts than one for such area, by such one of them as may be specified in this behalf by the High Court concerned.

Application of Code to proceeding before special court

Section 26D provides that the Code of Criminal Procedure, 1973 shall apply to the proceeding before a special court and for the purposes of the said provisions, the special court shall be deemed to be Court of Session and the person conducting prosecution before a special court shall be deemed to be a public prosecutor within the meaning of the Code of Criminal Procedure, 1973. The persons conducting prosecution should have been in practice as an Advocate for not less than seven years or shall have held a post, for a period of not less than seven years, under the Union or a State, requiring special knowledge of law.

RIGHTS OF INVESTORS

Entitlement of the Investors to Dividend declared by the Company

It shall be lawful for the holder of any security whose name appears on the books of the company issuing the said security to receive and retain any dividend declared by the company in respect thereof for any year, notwithstanding that the said security has already been transferred by him for consideration, unless the transferee who claims the dividend from the transferor has lodged the security and all other documents relating to the transfer which may be required by the company with the company for being registered in his name within fifteen days of the date on which the dividend became due.

Explanation. – The period specified in this section shall be extended –

- (i) in case of death of the transferee, by the actual period taken by his legal representative to establish his claim to the dividend;
- (ii) in case of loss of the transfer deed by theft or any other cause beyond the control of the transferee, by the actual period taken for the replacement thereof; and
- (iii) in case of delay in the lodging of any security and other documents relating to the transfer due to causes connected with the post, by the actual period of the delay.

Nothing contained in sub-section (1) shall affect –

- (a) the right of a company to pay any dividend which has become due to any person whose name is for the time being registered in the books of the company as the holder of the security in respect of which the dividend has become due; or
- (b) the right of the transferee of any security to enforce against the transferor or any other person his rights, if any, in relation to the transfer in any case where the company has refused to register the transfer of the security in the name of the transferee.

Right to Receive Income From Collective Investment Scheme

It shall be lawful for the holder of any securities, being units or other instruments issued by collective investment scheme, whose name appears on the books of the collective investment scheme issuing the said security to receive and retain any income in respect of units or other instruments issued by the collective investment scheme declared by the collective investment scheme in respect thereof for any year, though the said security, being units or other instruments issued by collective investment scheme, has already been transferred by him for consideration, unless the transferee who claims the income in respect of units or other instruments issued by collective investment scheme from the transfer or has lodged the security and all other documents relating to the transfer which may be required by the collective investment scheme with the collective investment scheme for being registered in his name within fifteen days of the date on which the income in respect of units or other instruments issued by the collective investments scheme became due.

Explanation – The period specified in this section shall be extended –

- (i) in case of death of the transferee, by the actual period taken by his legal representative to establish his claim to the income in respect of units or other instruments issued by collective investment scheme;
- (ii) in case of loss of the transfer deed by theft or any other cause beyond the control of the transferee, by the actual period taken for the replacement thereof; and
- (iii) in case of delay in the lodging of any security, being units or other instruments issued by the collective investment scheme, and other documents relating to the transfer due to causes connected with the post, by the actual period of the delay.

This shall not affect –

- (a) the right of a collective investment scheme to pay any income from units or other instruments issued by collective investment scheme which has become due to any person whose name is for the time being registered in the books of the collective investment scheme as the registered holder in the books of the collective investment scheme being units or other instruments issued by collective investment scheme in respect of which the income in respect of units or other instruments issued by collective scheme has become due; or
- (b) the right of transferee of any security, being units or other instruments issued by collective investment scheme, to enforce against the transferor or any other person his rights, if any, in relation to the transfer in any case where the company has refused to register the transfer of the security being units or other instruments issued by the collective investment scheme in the name of the transferee.

Right to receive Income from Mutual Fund

Section 27B provides that it shall be lawful for the holder of any securities, being units or other instruments issued by any mutual fund, whose name appears on the books of the mutual fund issuing the said security to receive and retain any income in respect of units or other instruments issued by the mutual fund declared by the mutual fund in respect thereof for any year, notwithstanding that the said security, being units or other instruments issued by the mutual fund, has already been transferred by him for consideration, unless the transferee who claims the income in respect of units or other instruments issued by the mutual fund from the transferor has lodged the security and all other documents relating to the transfer which may be required by the mutual fund with the mutual fund for being registered in his name within fifteen days of the date on which the income in respect of units or other instruments issued by the mutual fund became due.

The period specified in this Section may be extended –

- (i) in case of death of the transferee, by the actual period taken by his legal representative to establish his claim to the income in respect of units or other instrument issued by the mutual fund;
- (ii) in case of loss of the transfer deed by theft or any other cause beyond the control of transferee, by the actual period taken for the replacement thereof;
- (iii) in case of delay in the lodging of any security, being units or other instruments issued by the mutual fund, and other documents relating to the transfer due to cause connected with the post, by the actual period of the delay.

Sub-section (2) provides that nothing contained in Sub-section (1) shall affect –

- (a) the right of a mutual fund to pay any income from units or other instruments issued by the mutual fund which has become due to any person whose name is for the time being registered in the books of the mutual fund as the holder of the security being units or other instruments issued by the mutual fund in respect of which the income in respect of units or other instruments issued by mutual fund has become due; or
- (b) the right of transferee of any security, being units or other instruments issued by the mutual fund, to enforce against the transferor or any other person his rights, if any, in relation to the transfer in any case where the mutual fund has refused to register the transfer of the security being units or other instruments issued by the mutual fund in the name of the transferee.

POWER OF CENTRAL GOVERNMENT TO DELEGATE OR TO MAKE RULES

Section 29A of the Securities Contracts (Regulation) Act, 1956 provides that the Central Government may, by order published in the Official Gazette, direct that the powers (except the power under section 30) exercisable by it under any provision of this Act shall, in relation to such matters and subject to such conditions, if any, as may be specified in the order, be exercisable also by SEBI or the Reserve Bank of India constituted under section 3 of the Reserve Bank of India Act, 1934.

Section 30 empowers the Central Government to make rules for the purpose of carrying into effect the objects of this Act by notification in the Official Gazette.

In particular, and without prejudice to the generality of the foregoing power, such rules may provide for,

- (a) the manner in which applications may be made, the particulars which they should contain and the levy of a fee in respect of such applications;
- (b) the manner in which any inquiry for the purpose of recognizing any stock exchange may be made, the conditions which may be imposed for the grant of such recognition, including conditions as to the admission of members if the stock exchange concerned is to be the only recognised stock exchange in the area; and the form in which such recognition shall be granted;
- (c) the particulars which should be contained in the periodical returns and annual reports to be furnished to the Central Government;

- (d) documents which should be maintained and preserved under section 6 and the periods for which they should be preserved;
- (e) manner in which any inquiry by the governing body of a stock exchange shall be made under section 6;
- (f) the manner in which the bye-laws to be made or amended under this Act shall before being so made or amended be published for criticism;
- (g) the manner in which applications may be made by dealers in securities for licences under section 17, the fee payable in respect thereof and the period of such licences, the conditions subject to which licences may be granted, including conditions relating to the forms which may be used in making contracts, the documents to be maintained by licensed dealers and the furnishing of periodical information to such authority as may be specified and the revocation of licences for breach of conditions;
- (h) the requirements which shall be complied with –
 - (A) by public companies for the purpose of getting their securities listed on any stock exchange;
 - (B) by collective investment scheme for the purpose of getting their units listed on any stock exchange;
- (ha) the grounds on which the securities of a company may be delisted from any recognised stock exchange under sub-section (1) of Section 21A;
- (hb) the form in which an appeal may be filed before the Securities Appellate Tribunal under sub-section (2) of Section 21A and the fees payable in respect of such appeal;
- (hc) the form in which an appeal may be filed before the Securities Appellate Tribunal under Section 22A and the fees payable in respect of such appeal;
- (hd) the manner of inquiry under sub-Section (1) of Section 23-I;
- (he) the form in which an appeal may be filed before the Securities Appellate Tribunal under Section 23L and the fees payable in respect of such appeal.
- (i) any other matter which is to be or may be prescribed.

Every rule made under this Act shall be laid, as soon as may be after it is made, before each House of Parliament, while it is in session, for a total period of thirty days which may be comprised in one session or in two or more successive sessions, and if, before the expiry of the session immediately following the session or the successive sessions aforesaid, both Houses agree in making any modification in the rule or both Houses agree that the rule should not be made, the rule shall thereafter have effect only in such modified form or be of no effect, as the case may be; so, however, that any such modification or annulment shall be without prejudice to the validity of anything previously done under that rule.

SPECIAL PROVISIONS RELATED TO COMMODITY DERIVATIVES

Section 30A deals with following special provisions relating to commodity derivatives:-

- (1) This Act shall not apply to non-transferable specific delivery contracts.
 However, no person shall organise or assist in organising or be a member of any association in any area to which the provisions of section 13 have been made applicable (other than a stock exchange) which provides facilities for the performance of any non-transferable specific delivery contract by any party thereto without having to make or receive actual delivery to or from the other party to the contract or to or from any other party named in the contract.
- (2) Where in respect of any area, the provisions of section 13 have been made applicable in relation to commodity derivatives for the sale or purchase of any goods or class of goods, the Central Government may, by notification, declare that in the said area or any part thereof as may be specified in the notification all or any of the provisions of this Act shall not apply to transferable specific delivery contracts for the sale or purchase of the said goods or class of goods either generally, or to any class of such contracts in particular.

- (3) If the Central Government is of the opinion that in the interest of the trade or in the public interest it is expedient to regulate and control non-transferable specific delivery contracts in any area, it may, by notification in the Official Gazette, declare that all or any of the provisions of this Act shall apply to such class or classes of non-transferable specific delivery contracts in such area in respect of such goods or class of goods as may be specified in the notification, and may also specify the manner in which and the extent to which all or any of the said provisions shall so apply.

POWER OF SEBI TO MAKE REGULATIONS

Section 31 provides that without prejudice to the provisions contained in Section 30 of SEBI Act, 1992, SEBI may, by notification in the Official Gazette, make regulations consistent with the provisions of this Act and the rules made thereunder to carry out the purposes of this Act.

In particular, and without prejudice to the generality of the foregoing power, such regulations may provide for all or any of the following matter namely : (a) the manner, in which at least fifty-one per cent of equity share capital of a recognised stock exchange is held, within twelve months from the date of publication of the order under sub-section (7), of Section 4B by the public other than shareholders having trading rights under sub-section (8) of that section; (b) the eligibility criteria and other requirements under Section 17A; (c) The terms determined SEBI for settlement of proceeding under sub-section (2) of section 23JA and (d) any other matter which is required to be, or may be, specified by regulations or in respect of which provision is to be made by regulation.

Every regulation made under this Act shall be laid, as soon as may be after it is made, before each House of Parliament, while it is in session for a total period of thirty days which may be comprised in one session or in two or more successive sessions, and if, before the expiry of the session immediately following the session or the successive sessions aforesaid, both Houses agree in making any modification in the regulation or both Houses agree that the regulation should not be made, the regulation shall thereafter have effect only in such modified form or be of no effect, as the case may be; so, however, that any such modification or annulment shall be without prejudice to the validity of anything previously done under that regulation.

SECURITIES CONTRACT (REGULATION) (STOCK EXCHANGE AND CLEARING CORPORATIONS) REGULATIONS, 2012

With an intent to regulate recognition, ownership and governance in stock exchanges and clearing corporations, SEBI on June 20, 2012 notified the Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporations) Regulations, 2012.

With the notification of these Regulations, the Securities Contracts (Regulations) (Manner of Increasing and Maintaining Public shareholding in recognized Stock Exchanges) Regulations, 2006, which dealt only with the Stock Exchanges stand repealed.

Definitions

“**Associate**” in relation to a person shall include another person:

- (i) who, directly or indirectly, by himself, or in combination with other persons, exercises control over the first person;
- (ii) who holds more than fifteen per cent shares in the paid up equity capital of the first person;
- (iii) who is a holding company or a subsidiary company of the first person;
- (iv) who is a relative of the first person;
- (v) who is a member of a Hindu Undivided Family wherein the first person is also a member;
- (vi) such other cases where SEBI is of the view that a person shall be considered as an associate based on the facts and factors including the extent of control, independence, conflict of interest.

“**Commodity derivatives exchange**” means a recognized stock exchange which assists, regulates or controls

the business of buying, selling or dealing only in commodity derivatives and option in securities with the prior approval of SEBI.

“National commodity derivatives exchange” means a commodity derivatives exchange that is demutualized, has an electronic trading platform and is permitted to assist, regulate or control the business of buying, selling or dealing in commodity derivatives and option in securities with the prior approval of SEBI.

“Netting” means the determination by Clearing Corporation of net payment or delivery obligations of the clearing members of a recognised clearing corporation by setting off or adjustment of the inter se obligations or claims arising out of buying and selling of securities including the claims and obligations arising out of the termination by the Clearing Corporation or Stock Exchange, in such circumstances as the Clearing Corporation may specify in bye-laws, of the transactions admitted for settlement at a future date, so that only a net claim be demanded, or a net obligation be owed.”

“Public” includes any member or section of the public but does not include any trading member or clearing member or their associates and agents.

However, a public sector bank, public financial institution, an insurance company, mutual fund and alternative investment fund in public sector, that has associate(s) as trading members or clearing members, shall be deemed as public for the purposes of these regulations.

“Public interest director” means an independent director, representing the interests of investors in securities market and who is not having any association, directly or indirectly, which in the opinion of SEBI, is in conflict with his role.

“Shareholder director” means a director who represents the interest of shareholders, and elected or nominated by such shareholders who are not trading members or clearing members, as the case may be, or their associates and agents.

Recognition of Stock Exchanges and Clearing Corporations

As per the provisions of these Regulations, all Stock Exchanges and Clearing Corporations are required to apply for recognition by the SEBI. The Stock Exchanges which have been recognized under the Act as on the date of commencement of these Regulations, shall be deemed to have been recognized under these Regulations and all the provisions shall be applicable on them. The existing Clearing Corporations will continue for a period of 3 months from the date of applicability of these Regulations until an application made for the recognitions is disposed of.

The Regulations provides for manner of making application, fees, documents required and consideration for grant of recognition by SEBI. The regulations also provides for the period of recognition, regulatory fees as well as provisions with respect to renewal and withdrawal of recognition.

Networth Requirements

Recognised Stock Exchanges and Clearing Corporations are required to maintain minimum network requirements of Rs. 100 crores at all times. The existing recognized Stock Exchanges and Clearing Corporations are required to fulfill the network requirement within a maximum period of 3 years from the date of commencement of these Regulations. The limit is not applicable to an applicant performing clearing functions of a recognized stock exchange on the date of commencement of these regulations. It is further provided that the recognized Stock Exchange or the recognized Clearing Corporation shall not distribute profit in manner to its shareholders until specified network limit is achieved. Recognised stock exchange or clearing corporation is required to submit an audited network certificate from the statutory auditor on a yearly basis by the thirtieth day of September of every year for the preceeding financial year.

The eligible instruments for investment such as fixed deposits, central government securities and liquid schemes of debt mutual funds to the extent permissible, other instruments as may be specified by SEBI from time to time, and cash and bank balance, shall be considered as liquid assets, for the purpose of calculation of net worth of a clearing corporation.

Ownership of Stock Exchanges (Replace with the following)

As per the provisions of the Regulations, the shareholding or ownership of a stock exchange shall be as following:

Shareholder	Equity share holding limit
Equity Share Capital to be held by Public	Atleast 51% of paid up equity capital
Individual resident in India [either directly or indirectly and either individually or with person acting in concert (PAC)]	Not more than 5%
Further <ul style="list-style-type: none"> • Stock exchange • Depository • Banking company • Insurance company • Public Financial Institution (acquire or hold either directly or indirectly and either individually or with PAC) 	up to 15% of the paid up equity capital
An Individual resident outside India (either directly or indirectly and either individually or with PAC) shall acquire or hold	Not more than 5% of the paid up equity capital
However, - <ul style="list-style-type: none"> (i) a foreign stock exchange; (ii) a foreign depository; (iii) a foreign banking company; (iv) an foreign insurance company; and (v) a foreign commodity derivatives exchange, (may acquire or hold, either directly or indirectly, either individually or together with persons acting in concert) 	Upto 15 per cent of the paid up equity share capital of a recognised stock exchange.
All the residents outside India taken together	Not more than 49% of total paid up equity capital
No Clearing Corporation shall hold any right, stake or interest in any recognized Stock Exchange.	
Any person who directly or indirectly and either individually or with PAC acquires 2% or more in equity capital would require to apply for approval of SEBI within 15 days of such acquisition. If the approval is not granted the shares so acquired shall be forthwith divested. Shareholders of existing recognized Exchange holding more than 2% equity may apply for approval within 90 days of commencement of these Regulations.	
Stock exchange, Depository, Banking company, Insurance company, Public Financial Institution allowed to hold upto 15% equity capital, cannot acquire either directly or indirectly and either individually or with PAC any holding over and above 5% without the prior approval from SEBI.	
Every shareholder of the recognized Stock Exchange is required to be a Fit & Proper person.	
Every shareholder of the recognized Stock Exchange is required to be a Fit & Proper person.	

Ownership of Clearing Corporations

The provisions with respect to ownership and shareholding of recognized Clearing Corporations as similar to the aforesaid provisions as applicable to recognized Stock Exchanges except for as following:

- 51% or more equity share capital to be held by one or more recognized Stock Exchanges.
- A single Stock Exchange cannot hold more than 15% of equity share capital in one Clearing Corporation.

Governance of Stock Exchanges and Clearing Corporations

The provisions with respect to management and governance of recognized Stock Exchanges as well as Clearing Corporations are also provided in the Regulation broadly covering the following:

- Composition of Governance Board
- Guidelines for election of chairperson as well as number of public interest directors, appointment of Shareholder director, etc on the Governing Board.
- Conditions for appointment of Directors and the Managing director.
- Code of conduct for Directors and Key Managerial Personnel.
- Compensation and Tenure for Key Managerial Personnel.
- Segregation of regulatory department from other departments.
- Constitution of Oversight committee
- Constitution of Advisory Committee
- Constitution of Risk Management committee (in case of clearing corporations)
- To formulate and implement a comprehensive detail risk management policy.
- Appointment of compliance officer
- Transfer of Profits
- Transfer of penalties
- Disclosure and Corporate Governance norms.

As per section 23(7) of SECC Regulations, 2012 provides that:-

- a) No trading member or clearing member, or their associates and agents, irrespective of the stock exchange/clearing corporation of which they are members, shall be on the governing board of any recognised stock exchange or recognised clearing corporation.
- b) A person who is a director in an entity, that itself is a trading member or clearing member or has associate(s) as trading member(s) or clearing member(s) in terms of regulation 2(1) (b), he/she will be deemed to be trading member or clearing member.

However, a person will not be deemed to be clearing member and/or trading member or their associate for the purpose of these regulations, if he/she is on the board of a PFI or bank which is in Public Sector or which either has no identifiable ultimate promoter or the ultimate promoter is in Public Sector or has well diversified shareholding, and such PFI or bank or its associate is a clearing member and/or trading member.

- c) The appointment shall be subject to fulfilment of other requirements and satisfaction of SEBI.
- d) Recognised stock exchange and recognised Clearing Corporation, shall monitor and ensure the compliance of governance of stock exchanges and clearing corporations on continuous basis, to ensure

that directors appointed, on their governing board, do not get associated with trading member or clearing member after approval and appointment.

Listing of Securities

As per the provisions of the Regulations, a recognized stock exchange can apply for the listing of its securities on any recognized stock exchange other than itself if:

- It complies with the provisions of these regulations.
- It has completed 3 years of continuous trading operations immediately preceding the date of application of listing.
- It has the approval of SEBI.

Though as per the provisions of these Regulations, the securities of a recognized Clearing Corporation shall not be listed on a stock exchange.

The Regulations also requires securities of both the recognized Stock Exchanges as well as Clearing Corporations to be held in dematerialized form.

As per Regulation 45(2) of the SECC Regulations, 2012 –

- Ensuring holding of 51 per cent by public at all times by the listed stock exchange. The listed stock exchange shall disseminate the details of its shareholding with category wise breakup, on a continuous basis, on its website. Similarly, the stock exchange where the shares are listed, shall also display the above information.
- Ensuring that all shareholders are fit and proper.
- Ensuring that shareholders holding shares above 2 per cent are fit and proper. In addition to the criteria mentioned above, on acquisition of shares above 2 per cent, shall seek approval of SEBI within 15 days of acquisition as per Regulation 19(2) and those intending to acquire beyond 5 per cent as per Regulation 19(3) have to seek prior approval of SEBI.

Contribution to the Settlement Guarantee Fund

According to regulation 33 of SECC Regulations, 2012 states that the contribution to the Settlement Guarantee Fund or the Trade Guarantee Fund as specified in regulation 39 of SECC Regulations, 2012 shall be made by the recognised stock exchange, the recognised clearing corporation and the clearing members, in the manner as may be specified by SEBI from time to time.

In case of any shortfall in the Fund, the recognised clearing corporation and the recognised stock exchange shall replenish the Fund to the threshold level as may be specified by SEBI from time to time.

Investment Policy of Clearing Corporation

Regulation 40 of SECC Regulations, 2012 states that the utilization of profits and investments by recognised clearing corporations shall be in accordance with the norms specified by SEBI which is discussed below:

While framing the Investment policy, the clearing corporations shall consider the following principles –

- a) The investment policy of the clearing corporation, shall be built on the premise of highest degree of safety and least market risk.
- b) The investments shall be broadly in fixed deposits/central government securities and liquid schemes of debt mutual funds.

The clearing corporations shall align the investment policy in line with the principles for investment laid down above, subject to the following –

- a) Fixed deposit with banks [only those banks which have a net worth of more than INR 500 crore and are rated A1 (or A1+) or equivalent,]
- b) Central government securities; and
- c) Liquid schemes of debt mutual funds:
 - Investment in liquid scheme of debt mutual funds, shall not exceed a limit of 10 per cent of the total investible resources held by the clearing corporation, at any point in time.
 - In case the clearing corporation has investments in mutual funds beyond the limits specified above, then such excess investments shall be liquidated by the clearing corporation. Fresh investments by the clearing corporation beyond the threshold limit prescribed above are not permitted.

Risk Management Practices

- Clearing corporation shall not accept Fixed Deposit Receipts (FDRs) from trading/clearing members as collateral, which are issued by the trading/ clearing member themselves or banks who are associate of trading/ clearing member.

Explanation - for this purpose, 'associate' shall have the same meaning as defined under Regulation 2 (b) of SECC Regulations 2012.

- Trading/Clearing Members who have deposited their own FDRs or FDRs of associate banks shall replace such collateral, with other eligible collateral as per extant norms, within a period of six months from the date of issuance of the circular.

Disclosure by Clearing Corporation

In order to improve transparency in disclosing the regulatory orders and arbitration matters as issued by Clearing Corporation, the clearing corporations shall post all the past regulatory orders as well as arbitration and appellate awards (i.e., issued since June 20, 2012) on their websites within 30 days, while fresh orders should be uploaded immediately.

The Clearing Corporation shall disseminate information with respect to brief profile, qualification, areas of experience / expertise, number of arbitration matters handled, pre-arbitration experience, etc. of the arbitrators on their website and the status of the implementation of the norm in the monthly development report shall be communicate to SEBI.

SECURITIES CONTRACTS (REGULATION) RULES, 1957

These rules were made by the Central Government in exercise of the powers conferred by Section 30 of the Securities Contracts (Regulation) Act, 1956 and notified on 21st February, 1957.

Definition

“Public” means persons other than –

- (i) the promoter and promoter group;
- (ii) subsidiaries and associates of the company.

Explanation : Here “promoter” and “promoter group” shall have the same meaning as assigned to them under the SEBI (ICDR) Regulations, 2009.

“Public Sector Company” means a body corporate constituted by an Act of Parliament or any State Legislature and includes a government company.

“Public Shareholding” means equity shares of the company held by public including shares underlying the depository receipts if the holder of such depository receipts has the right to issue voting instruction and such depository receipts are listed on an international exchange in accordance with the Depository Receipts Scheme, 2014.

However, the equity shares of the company held by the trust set up for implementing employee benefit schemes under the regulations framed by SEBI shall be excluded from public shareholding.

Application for recognition

Under rules 3, it is laid down that an application under section 3 of the SCRA for recognition of a stock exchange shall be made to SEBI in Form A. This form is to be used for seeking recognition as well as renewal of recognition of a stock exchange. The annexure to form A requires the applicant stock exchange to furnish general information about itself and also details about its membership, governing body, trading and miscellaneous matters.

The application shall be accompanied by 4 copies of the rules (including the memorandum and articles of association where the applicant stock exchange is an incorporated body) and bye-laws of the stock exchange applying for recognition and the receipt obtained for payment of fees.

Before granting recognition to a stock exchange, SEBI may make such enquiries and require such further information to be furnished as it deems necessary, in relation to the information furnished in the Annexure to the application.

Form of Recognition

Rule 6 provides that the recognition granted to a stock exchange shall be in Form B and subject to the following conditions, namely –

- (a) that the recognition unless granted on a permanent basis, shall be for such period not less than one year as may be specified in the recognition;
- (b) that the stock exchange shall comply with such conditions as are or may be prescribed or imposed under the provisions of the Act and these rules from time to time.

In case of a recognised stock exchange, renewal of such recognition should be sought from SEBI not later than 3 months before expiry of the period of recognition.

In case SEBI desires to withdraw recognition from a stock exchange, SEBI shall first issue a show-cause notice in Form C and obtain information. Only after considering the submissions of the stock exchange SEBI can take a decision on withdrawal of recognition.

Qualification prescribed for Membership of a recognised Stock Exchange

Rule 8 contains detailed provisions on this subject and they are as follows:

No person shall be liable to be elected as a member if–

- (a) he is less than twenty-one years of age;
- (b) he is not a citizen of India;

However, the governing body may in suitable cases relax this condition with the prior approval of SEBI;

- (c) he has been adjudged bankrupt or a receiving order in bankruptcy has been made against him or he has been proved to be insolvent even though he has obtained his final discharge;

- (d) he has compounded with his creditors unless he has paid 100 paise in the rupee;
- (e) he has been convicted of an offence involving fraud or dishonesty;
- (f) he is engaged as principal or employee in any business other than that of securities or commodity derivatives except as a broker or agent not involving any personal financial liability unless he undertakes on admission to sever his connection with such business;

However no member may conduct business in commodity derivatives, except by setting up a separate company which shall comply with the regulatory requirements, such as, networth, capital adequacy, margins and exposure norms as may be specified by the Forward Market Commission, from time to time:

Further that nothing herein shall be applicable to any corporations, bodies corporate, companies or institutions referred to in items (a) to (n) of the proviso to sub-rule (4).

- (g) he has been at any time expelled or declared a defaulter by any other stock exchange;
- (h) he has been previously refused admission to membership unless a period of one year has elapsed since the date of such rejection.

No person eligible for admission as a member under sub-rule (1) shall be admitted as a member unless:

- (a) he has worked for not less than two years as a partner with, or as an authorised assistant or authorised clerk or remisier or apprentice to, a member; or
- (b) he agrees to work for a minimum period of two years as a partner or representative member with another member and to enter into bargains on the floor of the stock exchange and not in his own name but in the name of such other member; or
- (c) he succeeds to the established business of a deceased or retiring member who is his father, uncle, brother or any other person who is, in the opinion of the governing body, a close relative;

However the rules of the stock exchange may authorise the governing body to waive compliance with any of the foregoing conditions if the person seeking admission is in respect of means, position, integrity, knowledge and experience of business in securities, considered by the governing body to be otherwise qualified for membership;

No person who is a member at the time of application for recognition or subsequently admitted as a member shall continue as such if—

- (a) he ceases to be a citizen of India;

However this shall not affect those who are not citizens of India but who were members at the time of such application or were admitted subsequently under the provisions of clause (b) of sub-rule (1) of this rule, subject to their complying with all other requirements of this rule;

- (b) he is adjudged bankrupt or a receiving order in bankruptcy is made against him or he is proved to be insolvent;
- (c) he is convicted of an offence involving fraud or dishonesty;
- (d) he engages either as principal or employee in any business other than that of securities or commodity derivatives except as a broker or agent not involving any personal financial liability, provided that—
 - (i) the governing body may, for reasons, to be recorded in writing, permit a member to engage himself as principal or employee in any such business, if the member in question ceases to carry on business on the stock exchange either as an individual or as a partner in a firm.
 - (ii) in the case of those members who were under the rules in force at the time of such application permitted to engage in any such business and were actually so engaged on the date of such

application, a period of three years from the date of the grant of recognition shall be allowed for severing their connection with any such business,

- (iii) nothing herein shall affect members of a recognised stock exchange which are corporations, bodies corporate, companies or institution referred to in item (a) to (n) of the proviso to sub-rule (4).

Corporate Membership

Sub-rule 4 provides that a company as defined in the Companies Act, 2013, shall be eligible to be elected as a member of a stock exchange if –

- (i) such company is formed in compliance with the provisions of Companies Act, 2013.
- (ii) a majority of the directors of such company are shareholders of such company and also members of that stock exchange; and
- (iii) the directors of such company, who are members of that stock exchange, have ultimate liability in such company;

However where SEBI makes a recommendation in this regard, the governing body of a stock exchange shall, in relaxation of the requirements of this clause, admit as member the following corporations, bodies corporate companies or institutions, namely–

- (a) the Industrial Finance Corporation, established under the Industrial Finance Corporation Act, 1948;
- (b) the Industrial Development Bank of India, established under the Industrial Development Bank Act, 1964;
- (c) any insurance company granted registration by the Insurance Regulatory Development Authority under the Insurance Act, 1938;
- (d) the Unit Trust of India, established under the Unit Trust of India Act, 1963;
- (e) the Industrial Credit and Investment Corporation of India, a company registered under the Companies Act, 2013;
- (f) the subsidiaries of any of the corporations or companies specified in (a) to (f) and any subsidiary of the State Bank of India or any nationalised bank set up for providing merchant banking services, buying and selling securities and other similar activities;
- (g) any bank included in the second schedule to RBI Act, 1934;
- (h) the Export Import Bank of India, established under the Export Import Bank of India Act, 1981;
- (i) the National Bank for Agriculture and Rural Development, established under the National Bank for Agriculture and Rural Development Act, 1981 and
- (j) the National Housing Bank, established under the National Housing Bank Act, 1987.
- (k) Central Board of Trustees, Employees' Provident Fund, established under the Employees' Provident Funds and Miscellaneous Provisions Act, 1952.
- (l) any pension fund registered or appointed or regulated by the Pension Fund Regulatory and Development Authority under the Pension Fund Regulatory And Development Authority Act, 2013; and
- (m) any Standalone Primary Dealers authorised by the Reserve Bank of India constituted under the Reserve Bank of India Act, 1934.

According to sub-rule 4A a company as defined in the Companies Act, 2013, shall also be eligible to be elected as a member of a Stock Exchange if –

- (i) such company is formed in compliance with the provisions of section 3 of the said Act;
- (ii) such company undertakes to comply with such financial requirements and norms as may be specified by SEBI for the registration of such company under sub-section (1) of section 12 of SEBI Act, 1992;
- (iii) the directors of the company are not disqualified for being members of a stock exchange except clause (1) of sub-clause (b) and sub-clause (f) thereof or clause (3) except sub-clause (a) and sub-clause (f) thereof and the Director of the company had not held the offices of the Director in any company which had been a member of the stock exchange and had been declared defaulter or expelled by the stock exchange; and
- (iv) not less than two directors of the company are persons who possess a minimum two years' experience—
 - (a) in dealing in securities; or
 - (b) as portfolio managers; or
 - (c) as investment consultants.

Sub-rule 5 provides that where any member of a stock exchange is a firm, the provisions of sub-rules (1), (3) and (4), shall, so far as they can, apply to the admission or continuation of any partner in such firm.

Sub-rule 6 lays down that a limited liability partnership as defined in the Limited Liability Partnership Act, 2008, shall also be eligible to be elected its a member of a stock exchange if:

- (i) such “limited liability partnership” undertakes to comply with such financial requirements and norms as may be provided by SEBI for registration of such limited liability partnerships under sub-section (1) of section 12 of the SEBI Act, 1992;
- (ii) the designate partners of the ‘limited liability partnership’ are not disqualified from being members of a stock exchange under sub-rule (1) [except clause (b) and (f) thereof or sub-rule (3) except clause (a) and clause (f) thereof and the designated partners of the ‘limited liability partnership’ had not held the offices of Directors in any company or body corporate or partner in any firm or ‘limited liability partnership’, which had been a member of the stock exchange and had been declared defaulter or expelled by the stock exchange; and
- (iii) not less than two designated partners of the ‘limited liability partnership’ are persons who possess a minimum experience of two years:-
 - (a) in dealing in securities; or
 - (b) as portfolio managers; or
 - (c) as investment consultants.

Sub-rule 7 lays down that any provident fund represent by its trustees, of an exempted establishment under the Employee's Provident Funds and Miscellaneous Provisions Act, 1952, shall be also be eligible to be elected as a member of a stock exchange.

Regulation of transaction in the stock exchange

All contracts between the members of a recognised stock exchange shall be confirmed in writing and shall be enforced in accordance with the rules and bye-laws of the stock exchange of which they are members.

SEBI may nominate one or more persons not exceeding three in number, as member or members of the governing body of every recognised stock exchange. Such member or members shall enjoy the same status and powers as other members of the governing body.

After receiving the report of the result of an enquiry made under clause (b) of sub-section (3) of Section 6 of the

Act, SEBI may take such action as they deem proper and, in particular, may direct the governing body of the stock exchange to take such disciplinary action against the offending member, including fine, expulsion, suspension or any other penalty of a like nature not involving the payment of money, as may be specified by SEBI; notwithstanding anything to the contrary contained in the rules or bye-laws of the stock exchange concerned, the governing body shall give effect to the directions of SEBI in this behalf and shall not in any manner commute, revoke or modify the action taken in pursuance of such directions, without the prior approval of SEBI. SEBI may however, either on its own motion or on the representation of the member concerned, modify or withdraw its direction to the governing body.

Every member shall get his accounts audited by a chartered accountant whenever such audit is required by SEBI.

Books and documents to be maintained and preserved

(A) By every recognised stock exchange

Every recognised stock exchange shall maintain and preserve the following books of account and documents for a period of five years;

(1) Minute books of the meetings of –

- (a) members;
- (b) governing body;
- (c) any standing committee or committees of the governing body or of the general body of members.

Register of members showing their full names and addresses. Where any member of the –

- (1) Stock exchange is a firm,
- (2) Full names and addresses of all partners shall be shown.
- (3) Register of authorised clerks.
- (4) Register of remisiers of authorised assistants.
- (5) Record of security deposits.
- (6) Margin deposits book.
- (7) Ledgers.
- (8) Journals.
- (9) Cash Book.
- (10) Bank pass-book.

(B) By every member of a recognised stock exchange

Every member of a recognised stock exchange shall maintain and preserve the following books of account and documents for a period of five years;

- (a) Register of transactions (Sauda book).
- (b) Clients' ledger.
- (c) General ledger.
- (d) Journals.
- (e) Cash book.

- (f) Bank pass-book.
- (g) Documents register showing full particulars of shares and securities received and delivered.

Every member of a recognised stock exchange shall maintain and preserve the following documents for a period of two years;

- (a) Members' contract books showing details of all contracts entered into by him with other members of the same exchange or counter-foils or duplicates of memos of confirmation issued to such other members.
- (b) Counter-foils or duplicates of contract notes issued to clients.
- (c) Written consent of clients in respect of contracts entered into as principals.

Manner of Enquiry in the Affairs of Stock Exchange

Rule 16 lays down that any enquiry in relation to the affairs of the governing body of a recognised stock exchange or the affairs of any member in relation to the stock exchange can be conducted only by the person or persons appointed by SEBI under section 6(3)(b) of the Act. The person or persons so appointed are referred to as the inquiring authority.

The procedure relating to the conduct of inquiry is stated below –

- where the inquiring authority consists of two or more persons, one of them shall be appointed as the chairman or senior member thereof;
- the inquiring authority shall hand over a statement of issues to be inquired into to the governing body or the member concerned, as the case may be, who will be given a reasonable opportunity to state their or his side of the case;
- if any witness is called for examination, an opportunity shall be provided to the governing body or the member whose affairs are being inquired into, as the case may be, to cross-examine such witness;
- where the inquiring authority consists of more than one person, the views of the majority shall be deemed to represent the findings of such authority and, in the event of an equality of votes, the chairman or senior member shall have a casting vote;
- the inquiring authority shall submit its report in writing to the SEBI within the period specified in the order of appointment;
- temporary absence from any hearing or hearings of any member of the inquiring authority shall not vitiate its proceedings.

Where SEBI has directed the governing body of a stock exchange to make an inquiry, the governing body concerned shall appoint one or more members thereof to make the inquiry.

Submission of annual reports and periodical returns by stock exchanges to SEBI

These matters are regulated under rule 17 & 17A respectively.

Every recognised stock exchange shall (before the 31st day of January in each year or within such extended time as SEBI may, from time to time, allow), furnish to SEBI annually with a report about its activities during the (preceding calendar year), which shall *inter alia* contain detailed information about the following matters:

- (a) changes in rules and bye-laws, if any;
- (b) changes in the composition of the governing body;
- (c) any new sub-committees set up and changes in the composition of existing ones;

- (d) admissions, re-admissions, deaths or resignations of members;
- (e) disciplinary action against members;
- (f) arbitration of disputes (nature and number) between members and non-members;
- (g) defaults;
- (h) action taken to combat any emergency in trade;
- (i) securities listed and de-listed; and
- (j) securities brought on or removed from the forward list.

Every recognised stock exchange shall within one month of the date of the holding of its annual general meeting, furnish to SEBI with a copy of its audited balance sheet and profit and loss account for its preceding financial year.

Rule 17A necessitated that every recognised stock exchange shall furnish to SEBI periodical returns relating to –

- (i) the official rates for the securities enlisted thereon;
- (ii) the number of shares delivered through the clearing house;
- (iii) the making-up prices;
- (iv) the clearing house programmes;
- (v) the number of securities listed and de-listed during the previous three months;
- (vi) number of securities brought on or removed from the forward list during the previous three months; and
- (vii) any other matter as may be specified by the SEBI.

REQUIREMENTS OF LISTING OF SECURITIES WITH RECOGNISED STOCK EXCHANGES

This is one of the most important provision of the Securities Contracts (Regulation) Rules, 1957. Rule 19 provides for the complete procedure in this regard. A public company as defined under the Companies Act, 2013, desirous of getting its securities listed on a recognised stock exchange, shall apply for the purpose to the stock exchange and forward along with its application the following documents and particulars:

- (a) Memorandum and articles of association and, in the case of a debenture issue, a copy of the trust deed.
- (b) Copies of all prospectuses or statements in lieu of prospectuses issued by the company at any time.
- (c) Copies of offers for sale and circulars or advertisements offering any securities for subscription or sale during the last five years.
- (d) Copies of balance sheets and audited accounts for the last five years, or in the case of new companies, for such shorter period for which accounts have been made up.
- (e) A statement showing –
 - (i) dividends and cash bonuses, if any, paid during the last ten years (or such shorter period as the company has been in existence, whether as a private or public company),
 - (ii) dividends or interest in arrears, if any.
- (f) Certified copies of agreements or other documents relating to arrangements with or between –

- (i) vendors and/or promoters,
- (ii) underwriters and sub-underwriters,
- (iii) brokers and sub-brokers.
- (g) Certified copies of agreements with –
 - (i) managing agents and secretaries and treasurers.
 - (ii) selling agents,
 - (iii) managing directors and technical directors,
 - (iv) general manager, sales manager, managers or secretary.
- (h) Certified copy of every letter, report, balance sheet, valuation contract, court order or other document, part of which is reproduced or referred to in any prospectus, offer for sale, circular or advertisement offering securities for subscription or sale, during the last five years.
- (i) A statement containing particulars of the dates of, and parties to all material contracts, agreements (including agreements for technical advice and collaboration), concessions and similar other documents (except those entered into in the ordinary course of business carried on or intended to be carried on by the company) together with a brief description of the terms, subject-matter and general nature of the documents.
- (j) A brief history of the company since its incorporation giving details of its activities including any reorganization, reconstruction or amalgamation, changes in its capital structure (authorised, issued and subscribed) and debenture borrowings, if any.
- (k) Particulars of shares and debentures issued (i) for consideration other than cash, whether in whole or part, (ii) at a premium or discount, or (iii) in pursuance of an option.
- (l) A statement containing particulars of any commission, brokerage, discount or other special terms including an option for the issue of any kind of the securities granted to any person.
- (m) Certified copies of –
 - (i) acknowledgment card or the receipt of filing offer document with the SEBI;
 - (ii) agreements, if any, with the Industrial Finance Corporation, Industrial Credit and Investment Corporation and similar bodies.
- (n) Particulars of shares forfeited.
- (o) A list of highest ten holders of each class or kind of securities of the company as on the date of application along with particulars as to the number of shares or debentures held by and the address of each such holder.
- (p) Particulars of shares or debentures for which permission to deal is applied for;

However, a recognised stock exchange may either generally by its bye-laws or in any particular case call for such further particulars or documents as it deems proper.

Rule 19(2)

Sub-rule 2 of Rule 19 provides that apart from complying with such other terms and conditions as may be laid down by a recognised stock exchange, an applicant company shall satisfy the stock exchange that;

Rule 19(2)(a)

(a) Its articles of association provide for the following among others –

- (i) that the company shall use a common form of transfer;
- (ii) that the fully paid shares will be free from all lien, while in the case of partly paid shares, the company's lien, if any, will be restricted to moneys called or payable at a fixed time in respect of such shares;
- (iii) that any amount paid-up in advance of calls on any share may carry interest but shall not entitle the holder of the share to participate in respect thereof, in a dividend subsequently declared;
- (iv) there will be no forfeiture of unclaimed dividends before the claim becomes barred by law;
- (v) that option or right to call of shares shall not be given to any person except with the sanction of the company in general meeting;

However, a recognised stock exchange may provisionally admit to dealings the securities of a company which undertakes to amend its articles of association at its next general meeting so as to fulfill the foregoing requirements and agrees to act in the meantime strictly in accordance with the provisions of this clause.

Rule 19(2)(b)

(b) The minimum offer and allotment to public in terms of an offer document shall be-

- (i) at least twenty five per cent of each class or kind of equity shares or debenture convertible into equity shares issued by the company, if the post issue capital of the company calculated at offer price is less than or equal to one thousand six hundred crore rupees;
- (ii) at least such percentage of each class or kind of equity shares or debentures convertible into equity shares issued by the company equivalent to the value of four hundred crore rupees, if the post issue capital of the company calculated at offer price is more than one thousand six hundred crore rupees but less than or equal to four thousand crore rupees;
- (iii) at least ten per cent of each class or kind of equity shares or debentures convertible into equity shares issued by the company, if the post issue capital of the company calculated at offer price is above four thousand crore rupees.

However, the company referred to in sub-clause (ii) or sub-clause (iii), shall increase its public shareholding to at least twenty five per cent within a period of three years from the date of listing of the securities, in the manner specified by the Securities and Exchange Board of India.

Further this clause shall not apply to a company whose draft offer document is pending with SEBI before the commencement of the Securities Contracts (Regulation) Third Amendment Rules, 2014, if it satisfies the conditions prescribed in clause (b) of sub-rule (2) of rule 19 of the Securities Contracts (Regulation) Rules, 1956 as existed prior to the date of such commencement.

Conditions precedent to submission of application for listing by stock exchange

Sub-rule (3) of Rule 19 deals with the conditions required to be fulfilled by a company precedent to listing company applying for listing shall, as conditions precedent, undertake *inter alia* –

- (a) (i) that letters of allotment will be issued simultaneously and that, in the event of its being impossible to issue letters of regret at the same time, a notice to that effect will be inserted in the press so that it will appear on the morning after the letters of allotment have been posted.

- (ii) that letters of right will be issued simultaneously,
 - (iii) that letters of allotment, acceptance or rights will be serially numbered, printed on good quality paper and, examined and signed by a responsible officer of the company and that whenever possible, they will contain the distinctive numbers of the securities to which they relate.
 - (iv) that letters of allotment and renounceable letters of right will contain a proviso for splitting and that, when so required by the exchange, the form of renunciation will be printed on the back of or attached to the letters of allotment and letters of right.
 - (v) that letters of allotment and letters of right will state how the next payment of interest or dividend on the securities will be calculated;
- (b) to issue, when so required, receipts for all securities deposited with it whether for registration, sub-division, exchange or for other purposes; and not to charge any fees for registration of transfers, for sub-division and consolidation of certificates and for sub-division of letters of allotment, renounceable letters of right, and split consolidation, renewal and transfer receipts into denominations of the market unit of trading;
- (bb) to issue, when so required, consolidation and renewal certificates in denominations of the market unit of trading, to split certificates, letters of allotment, letters of right, and transfer, renewal, consolidation and split receipts into smaller units, to split call notices, issue duplicates thereof and not require any discharge on call receipts and to accept the discharge of members of stock exchange on split, consolidation and renewal receipts as good and sufficient without insisting on the discharge of the registered holders;
- (c) when documents are lodged for sub-division or consolidation (or renewal) through the clearing house of the exchange;
- (i) to accept the discharge of an official of the stock exchange clearing house on the company's split receipts and (consolidation receipts and renewal receipts) as good and sufficient discharge without insisting on the discharge of the registered holders; and
 - (ii) to verify when the company is unable to issue certificates or split receipt or (consolidation receipts or renewal receipts) immediately on lodgement whether the discharge of the registered holders, on the documents lodged for sub-division or consolidation (or renewal) and their signatures on the relative transfers are in order;
- (d) on production of the necessary documents by shareholders or by members of the exchange, to make on transfers an endorsement to the effect that the power of attorney or probate or letters of administration or death certificate or certificate of the Controller of Estate Duty or similar other document has been duly exhibited to and registered by the company;
- (e) to issue certificates in respect of shares or debentures lodged for transfer within a period of one month of the date of lodgement of transfer and to issue balance certificates within the same period where the transfer is accompanied by a larger certificate;
- (f) to advise the stock exchange of the date of the board meeting at which the declaration or recommendation of a dividend (or the issue or right or bonus share) will be considered;
- (g) to recommend or declare all dividends and/or cash bonuses at least five days before the commencement of the closure of its transfer books or the record date fixed for the purpose and so advise the stock exchange in writing of all dividends and/or cash bonuses recommended or declared immediately after a meeting of the board of the company has been held to finalise the same;

- (h) to notify the stock exchange of any material change in the general character or nature of the company's business;
- (i) to notify the stock exchange of any change –
 - (i) in the company's directorate by death, resignation, removal or otherwise,
 - (ii) of managing director, managing agent or secretaries and treasurers,
 - (iii) of auditors appointed to audit the books and accounts of the company;
- (j) to forward to the stock exchange copies of statutory and annual reports and audited accounts as soon as issued, including directors' reports;
- (k) to forward to the stock exchange as soon as they are issued, copies of all other notices and circulars sent to the shareholders including proceedings of ordinary and extraordinary general meetings of the company and to file with the stock exchange certified copies of resolutions of the company as soon as such resolutions become effective;
- (l) to notify the stock exchange prior to intimating the shareholders, of any new issue of securities whether by way of right, privilege, bonus or otherwise and the manner in which it is proposed to offer or allot the same;
- (m) to notify the stock exchange in the event of re-issue of any forfeited securities or the issue of securities held in reserve for future issue;
- (n) to notify the stock exchange of any other alteration of capital including calls;
- (o) to close the transfer books only for the purpose of declaration of dividend or issue of right or bonus shares or for such other purposes as the stock exchange may agree and to give notice to the stock exchange as many days in advance as the exchange may from time to time reasonably prescribe, stating the dates of closure of its transfer books (or, when the transfer books are not to be closed, the date fixed for taking a record of its shareholders or debenture holders) and specifying the purpose or purposes for which the transfer books are to be closed (or the record is to be taken) and in the case of a right or bonus issue to so close the transfer books or fix a record date only after the sanctions of the competent authority subject to which the issue is proposed to be made have been duly obtained, unless the exchange agrees otherwise;
- (p) to forward to the stock exchange an annual return immediately after each annual general meeting of at least ten principal holders of each class of security of the company along with particulars as to the number of shares or debentures held by, and address of, each such holder;
- (q) to grant to shareholders the right of renunciation in all cases of issue of rights, privileges and benefits and to allow them reasonable time not being less than four weeks within which to record, exercise, or renounce such rights, privileges and benefits, and to issue, where necessary, coupons or fractional certificates or provide for the payment of the equivalent of the value of the fractional right in cash unless the company in general meeting or the stock exchange agrees otherwise;
- (r) to promptly notify the stock exchange–
 - (i) of any action which will result in the redemption, cancellation or retirement in whole or in part of any securities listed on the exchange,
 - (ii) of the intention to make a drawing of such securities, intimating at the same time the date of the drawing and the period of the closing of the transfer books (or the date of the striking of the balance) for the drawing;

- (iii) of the amount of securities outstanding after any drawing has been made;
- (s) to intimate the stock exchange any other information necessary to enable the shareholders to appraise the position of the company and to avoid the establishment of a false market in the shares of the company;
- (t) that in the event of the application for listing being granted, such listing shall be subject to the rules and bye-laws of the exchange in force from time to time and that the company will comply within a reasonable time, with such further listing requirements as may be promulgated by the exchange as a general condition for new listings.

Application for listing of new securities

An application for listing shall be necessary in respect of the following:

- (a) all new issues of any class or kind of securities of a company to be offered to the public;
- (b) all further issues of any class or kind of securities of a company if such class or kind of securities of the company are already listed on a recognised stock exchange. **[Rule 19(4)]**

Suspension or withdrawal of admission to dealings in securities on stock exchange

A recognised stock exchange may suspend or withdraw admission to dealings in the securities of a company or body corporate either for a breach of or non-compliance with, any of the conditions of admission to dealings or for any other reason, to be recorded in writing, which in the opinion of the stock exchange justifies such action;

However, no such action shall be taken by a stock exchange without affording to the company or body corporate concerned a reasonable opportunity by a notice in writing, stating the reasons, to show cause against the proposed action;

Further that where a recognised stock exchange has withdrawn admission to dealings in any security, or where suspension of admission to dealings has continued for a period exceeding three months, the company or body corporate concerned may prefer an appeal to the Securities Appellate Tribunal constituted under section 15K of the SEBI Act, 1992 and the procedure laid down under the Securities Contracts (Regulation) (Appeal to Securities Appellate Tribunal) Rules, 2000 shall apply to such appeal. The Securities Appellate Tribunal may, after giving the stock exchange an opportunity of being heard, vary or set aside the decision of the stock exchange and its orders shall be carried out by the stock exchange.

A recognised stock exchange may, either at its own discretion or shall in accordance with the orders of the Securities Appellate Tribunal restore or re-admit to dealings any securities suspended or withdrawn from the list.

All requirements with respect to listing prescribed by these rules shall, so far as they may be, also apply to a public sector company.

SEBI may, at its own discretion or on the recommendation of a recognised stock exchange, waive or relax the strict enforcement of any or all of the requirements with respect to listing prescribed by these rules. **[Rule 19(5)]**

CONTINUOUS LISTING REQUIREMENT

Rule 19A (1) stipulates that every listed company other than public sector company shall maintain public shareholding of at least 25%.

However, any listed company which has public shareholding below 25%, shall increase its public shareholding

to at least twenty five per cent, within a period of four years from the date of commencement of amendment to the said rules in 2014, in the manner specified by SEBI.

Explanation : For the purposes of this sub-rule, a company whose securities has been listed pursuant to an offer and allotment made to public in terms of sub-clause (ii) of clause (b) of sub-rule (2) of rule 19, shall maintain minimum 25% public shareholding from the date on which the public shareholding in the company reaches the level of 25% in terms of said sub-clause.

Sub-rule (2) provides that where the public shareholding in a listed company falls below 25 % at any time, such company shall bring the public shareholding to 25% within a maximum period of twelve months from the date of such fall in the manner specified by SEBI.

Where the public shareholding in a listed company falls below 25% in consequence to SCRR Amendment Rules, 2015, such company shall increase its shareholding to atleast 25%, in the manner specified by SEBI within a period of three years, as the case may be, from the date of notification of:

- (a) the Depository Receipts Scheme, 2014, in cases where the public shareholding falls below 25% as a result of such Scheme;
- (b) SEBI (Share Based Employee Benefits) Regulations, 2014, in cases where the public shareholding falls below 25%, as a result of such regulations.

DELISTING OF SECURITIES

Rule 21 deals with delisting of Securities. A recognized stock exchange may, without prejudice to any other action that may be taken under the Act or under any other law for the time being in force, delist any securities listed thereon on any of the following grounds in accordance with the regulations made by SEBI, namely:—

- (a) the company has incurred losses during the preceding three consecutive years and it has negative network;
- (b) trading in the securities of the company has remained suspended for a period of more than six months;
- (c) the securities of the company have remained infrequently traded during the preceding three years;
- (d) the company or any of its promoters or any of its director has been convicted for failure to comply with any of the provisions of the Act or SEBI Act, 1992 or the Depositories Act, 1996 or rules, regulations, agreements made thereunder, as the case may be and awarded a penalty of not less than rupees one crore or imprisonment of not less than three years;
- (e) the addresses of the company or any of its promoter or any of its directors, are not known or false addresses have been furnished or the company has changed its registered office in contravention of the provisions of the Companies Act, 2013, or;
- (f) shareholding of the company held by the public has come below the minimum level applicable to the company as per the listing agreement under the Act and the company has failed to raise public holding to the required level within the time specified by the recognized stock exchange.

However, no securities shall be delisted unless the company concerned has been given a reasonable opportunity of being heard.

(2) If the securities is delisted under clause (1),

- (a) the company, promoter and director of the company shall be jointly and severally liable to purchase the outstanding securities from those holders who wish to sell them at a fair price determined in accordance with regulations made by SEBI, under the Act; and
- (b) the said securities shall be delisted from all recognized stock exchanges.

(3) A recognized stock exchange may, on the request of the company, delist any securities listed thereon in accordance with the regulations made under the Act by SEBI, subject to the following conditions, namely :

- (a) the securities of the company have been listed for a minimum period of three years on the recognized stock exchange;
- (b) the delisting of such securities has been approved by the two-third of public shareholders; and
- (c) the company, promoter and/or the director of the company purchase the outstanding securities from those holders who wish to sell them at a price determined in accordance with regulations made by SEBI under the Act.

However, the condition at (c) may be dispensed with by SEBI if the securities remain listed at least on the National Stock Exchange of India Limited or the Bombay Stock Exchange Limited.

LESSON ROUND UP

- The Securities Contracts (Regulation) Act, 1956 was enacted by Parliament to prevent undesirable transactions in securities by regulating the business of dealing therein, and by providing for certain other matters connected therewith.
- Section 2 of this Act contains definitions of various terms used in the Act.
- Section 17A of the Act provides for public issue and listing of securities.
- The Act prescribes various penalties against persons who might be found guilty of offences under the Act.
- Section 21 of the Act provides that where securities are listed on the application of any person in any recognised stock exchange, such person shall comply with the conditions of the listing agreement with that stock exchange.
- Section 31 provides that without prejudice to the provisions contained in Section 30 of SEBI Act, 1992, SEBI may, by notification in the Official Gazette, make regulations consistent with the provisions of this Act and the rules made thereunder to carry out the purposes of this Act.
- With an Intent to regulate recognition, ownership, and governance in stock exchange and cleaning corporations, SEBI on June 20, 2012 issued the Securities Contracts (Regulation) (Stock Exchanges and Clear Corporations) Regulations, 2012.
- The Government promulgated the Securities Contracts (Regulation) Rules, 1957 for carrying into effect the object of the SCRA Act, 1956.
- Rule 19 dealt with the requirement with respect to the listing of securities on a recognised stock exchange. Rule 19A provides the detailed provision regarding continuous listing agreement.

GLOSSARY

Demutualization	Process from “mutually owned” association to a company “owned by shareholders”. In other words, transformation of the legal structure from a mutual from to a business corporation form and privatisation of the corporations so constituted is referred to as demutualization.
Stock Exchange	Anybody of individuals, whether incorporated or not, constituted for the purpose of assisting, regulating controlling the business of buying, selling or dealing in securities.
Appointed date	It means the date which SEBI may, by notification in the Official Gazette, appoint

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation.)

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- This image shows a blank sheet of white paper with horizontal ruling lines. The lines are evenly spaced and extend across the width of the page. There is a solid black rectangular bar at the top edge of the image.

Lesson 17

Securities and Exchange Board of India

LESSON OUTLINE

- Introduction
- Objective of SEBI
- Securities and Exchange Board of India Act, 1992
- Composition of SEBI
- Powers and functions of Securities and Exchange Board of India
- Investigations Procedure
- Penalties for failure, default, contravention
- Securities Appellate Tribunal
- Establishment, Composition of Securities Appellate Tribunal
- Procedures & Powers of Securities Appellate Tribunal
- Legal representation
- Appeal to Supreme Court
- Powers of Central Government
- SEBI's (Settlement of Administrative & Civil Proceedings) Regulations, 2014
- SEBI (Procedure for Search and Seizure) Regulations, 2014
- LESSON ROUND UP
- GLOSSARY
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

Securities and Exchange Board of India (SEBI) has been established with two objectives of protecting the interest of investors and to promote the development of and to regulate the Securities Market. Since its establishment in 1992 lot of initiatives have been taken to protect the interests of Indian investors.

In this lesson, the student will be able to know the powers and functions of SEBI; provisions relating to regulation of financial intermediaries, penalties for insider trading and fraudulent practices, promoting investors education and training and inspection of various regulated entities, procedure for filing appeal with the Securities Appellate Tribunal, and establishment of special court for speedy trial of offences consent order mechanism etc.

INTRODUCTION

Before 1992, the three principal Acts governing the securities markets were:

(a) the Capital Issues (Control) Act, 1947, which restricted issuer's access to the securities market and controlled the pricing of issues; (b) the Companies Act, 1956, which sets out the code of conduct for the corporate sector in relation to issue, allotment and transfer of securities, and disclosures to be made in public issues; and (c) the Securities Contracts (Regulation) Act, 1956, which provides for regulation of transactions in securities through control over stock exchanges. The Capital Issues (Control) Act, 1947 had its origin during the war in 1943 when the objective was to channel resources to support the war effort. The Act was retained with some modifications as a means of controlling the raising of capital by companies and to ensure that national resources were channelled into proper lines, i.e., for desirable purposes to serve goals and priorities of the government, and to protect the interests of investors. Under the Act, any firm wishing to issue securities had to obtain approval from the Central Government, which also determined the amount, type and price of the issue.

Major part of the liberalisation process was the repeal of the Capital Issues (Control) Act, 1947 in May 1992. With this, Government's control over issue of capital, pricing of the issues, fixing of premia and rates of interest on debentures etc. ceased. The office which administered the Act was abolished and the market was allowed to allocate resources to competing uses. However to ensure effective regulation of the market, SEBI Act, 1992 was enacted to empower SEBI with statutory powers for (a) protecting the interests of investors in securities, (b) promoting the development of the securities market, and (c) regulating the securities market. Its regulatory jurisdiction extends over corporates in the issuance of capital and transfer of securities, in addition to all intermediaries and persons associated with securities market. SEBI can specify the matters to be disclosed and the standards of disclosure required for the protection of investors in respect of issues; can issue directions to all intermediaries and other persons associated with the securities market in the interest of investors or of orderly development for securities market; and can conduct enquiries, audits and inspection of all concerned and adjudicate offences under the Act. In short, it has been given necessary autonomy and authority to regulate and develop an orderly securities market.

OBJECTIVE OF SEBI

- To protect the interests of investors in securities
- To promote the development of, and
- To regulate, the securities market and for matters connected therewith or incidental thereto.

SEBI ACT, 1992

Chapter I of the Act covers the definitions of various terms under the Act, while Chapter II deals with establishment of SEBI and its management. In terms of section 3 of the Act, SEBI is a body corporate having perpetual succession and a common seal with power to acquire, hold and dispose of property, both movable and immovable and to contract, sue and be sued in its own name. SEBI has its Head Office at Mumbai and has powers to establish its offices at other places in India.

COMPOSITION OF SEBI

Section 4(1) of SEBI Act provides that the SEBI shall consist of the following members, namely:

- (a) a Chairman;
- (b) two members from amongst the officials of the Ministry of the Central Government dealing with Finance and administration of the Companies Act, 2013;
- (c) one member from amongst the officials of the Reserve Bank;

- (d) five other members of whom at least three shall be the whole time members, to be appointed by the Central Government.

The Chairman and the other members shall be persons of ability, integrity and standing who have shown capacity in dealing with problems relating to securities market or have special knowledge or experience of law, finance, economics, accountancy, administration or in any other discipline which, in the opinion of the Central Government, shall be useful to SEBI.

The terms and conditions of service of Chairman and members are determined in the rules framed by Government in this regard.

The general superintendence, direction and management of the affairs of SEBI vests in a Board of members, which may exercise all powers and do all acts and things which may be exercised or done by SEBI. Unless determined otherwise through regulations, the Chairman shall also have all these powers.

POWERS AND FUNCTIONS OF SEBI

Chapter IV of SEBI Act, 1992 deals with the powers and functions of SEBI. Section 11 of the Act lays down that it shall be the duty of SEBI to protect the interests of the investors in securities and to promote the development of, and to regulate the securities markets by such measures as it thinks fit. Section 11(2) provides that these measures would include:

- (a) regulating the business in stock exchanges and any other securities markets;
- (b) registering and regulating the working of stock brokers, sub-brokers, share transfer agents, bankers to an issue, trustees of trust deeds, registrars to an issue, merchant bankers, underwriters, portfolio managers, investment advisers and such other intermediaries who may be associated with securities markets in any manner;
- (ba) registering and regulating the working of the depositories, participants, custodians of securities, foreign institutional investors, credit rating agencies and such other intermediaries as SEBI may, by notification, specify in this behalf;
- (c) registering and regulating the working of venture capital funds and collective investment schemes, including mutual funds;
- (d) promoting and regulating self-regulatory organisations;
- (e) prohibiting fraudulent and unfair trade practices relating to securities markets;
- (f) promoting investors' education and training of intermediaries of securities markets;
- (g) prohibiting insider trading in securities;
- (h) regulating substantial acquisition of shares and takeover of companies;
- (i) calling for information from, undertaking inspection, conducting inquiries and audits of the stock exchanges, mutual funds, other persons associated with the securities market, intermediaries and self-regulatory organisations in the securities market;
- (ia) calling for information and records from any person including any bank or any authority or board or corporation established or constituted by or under any central or state Act, which in the opinion of SEBI, shall be relevant to any investigation or inquiry by SEBI in respect of any transaction in securities.
- (ib) calling for information from or furnishing information to other authorities. Whether in India, or outside India having functions similar to those of SEBI, in the matters relating to the prevention or detection of violation in respect of securities laws, subject to the provisions of other laws for the time being in force in this regard.

However, SEBI for the purpose of furnishing any information to any authority outside India, may enter

into an arrangement or agreement or understanding with such authority with approval of the Central Government.

- (j) performing such functions and exercising such powers under the provisions of the Securities Contracts (Regulation) Act, 1956, as may be delegated to it by the Central Government;
- (k) levying fees or other charges for carrying out the purposes of this section;
- (l) conducting research for the above purposes;
- (la) calling from or furnishing to any such agencies, as may be specified by SEBI, such information as may be considered necessary by it for the efficient discharge of its functions;
- (m) performing such other functions as may be prescribed.

Section 11(2A) prescribed that SEBI may take measures to undertake inspection of any book, or register, or other document or record of any listed public company or a public company (not being intermediaries referred to in section 12) which intends to get its securities listed on any recognised stock exchange where SEBI has reasonable grounds to believe that such company has been indulging in insider trading or fraudulent and unfair trade practices relating to securities market.

Section 11(3) of SEBI Act provides that for carrying out the duties assigned to it under the Act, SEBI has been vested with the same powers as are available to a Civil Court under the Code of Civil Procedure, 1908 for trying a suit in respect of the following matters:

- (i) the discovery and production of books of account and other documents at such place and such time indicated by SEBI.
- (ii) summoning and enforcing the attendance of persons and examining them on oath.
- (iii) inspection of any books, registers and other documents of any person listed in section 12 of the Act, namely stock brokers, sub brokers, share transfer agents, bankers to an issue, trustee of trust deed, registrar to an issue, merchant bankers, underwriters, portfolio managers, investment advisors and other such intermediaries associated with securities markets at any place.
- (iv) inspection of any book or register or other document or record of any listed company or a public company which intends to get its securities listed on any recognized stock exchange.
- (v) issuing commissions for the examination of witnesses or documents.

As per Section 11(4) SEBI, may, by an order or for reasons to be recorded in writing, in the interest of investors or securities market take any of the following measures either pending investigation or inquiry or on completion of such investigation or enquiry namely:

- (a) suspend the trading of any security in a recognised stock exchange.
- (b) restrain persons from accessing the securities market and prohibit any person associated with securities market to buy, sell or deal in securities.
- (c) suspend any office-bearer of any stock exchange or self regulatory organisation from holding such position.
- (d) impound and retain the proceeds or securities in respect of any transaction which is under investigation.
- (e) attach for a period not exceeding one month, with prior approval of a magistrate of the first class having jurisdiction, one or more bank accounts of any intermediary or any person associated with the securities market in any of the Act or rules or regulations made thereunder.

However, only the bank account or accounts or any transaction entered therein, so far as it relates to the proceeds actually involved in violation of any of the provisions of this Act, or the rules or regulations made there under shall be allowed to be attached.

- (f) direct any intermediary or any person associated with the securities market in any manner not to dispose of or alienate an asset forming part of any transaction which is under investigation.

SEBI may take any of the measures specified in clause (d) or clause (e) or clause (f) in respect of any listed public company or a public company not being an intermediary which intends to get its securities listed on any recognised stock exchange where SEBI has reasonable grounds to believe that such company has been indulging in insider trading or fraudulent and unfair trade practices relating to securities market. Further, SEBI shall, either before or after passing such orders, give an opportunity of being heard to such intermediaries or persons concerned.

Section 11(5) of the Act authorises SEBI to disgorge the amount, pursuant to direction issued under section 11B or section 12A of the Securities Contracts (Regulation) Act, 1956 or section 19 of the Depositories Act, 1996, as the case may be, shall be credited to the Investor Protection and Education Fund established by SEBI and such amount shall be utilized by SEBI in accordance with the regulations made under this Act.

TO REGULATE OR PROHIBIT ISSUE OF PROSPECTUS, OFFER DOCUMENT OR ADVERTISEMENT SOLICITING MONEY FOR ISSUE OF SECURITIES

Section 11A(1) of SEBI Act, 1992 provides that without prejudice to the provisions of the Companies Act, 2013, SEBI may, for the protection of investors, –

- (a) specify, by regulations –
 - (i) the matters relating to issue of capital, transfer of securities and other matters incidental thereto; and
 - (ii) the manner in which such matters shall be disclosed by the companies;
- (b) by general or special orders –
 - (i) prohibit any company from issuing prospectus, any offer document, or advertisement soliciting money from the public for the issue of securities;
 - (ii) specify the conditions subject to which the prospectus, such offer document or advertisement, if not prohibited, may be issued.

Without prejudice to the provisions of section 21 of the Securities Contracts (Regulation) Act, 1956, SEBI may specify the requirements for listing and transfer of securities and other matters incidental thereto.

POWER TO ISSUE DIRECTIONS

Section 11B of the Act provides that if SEBI is satisfied after making due enquiries, that it is necessary:

- (i) in the interest of investors, or orderly development of securities market; or
- (ii) to prevent the affairs of any intermediary or other persons referred to in section 12 being conducted in a manner detrimental to the interests of investors or securities market; or
- (iii) to secure the proper management of any such intermediary or person,

SEBI may issue such directions, –

- (a) to any person or class of persons referred to in section 12, or associated with the securities market; or
- (b) to any company in respect of matters relating to issue of capital, transfer of securities and other matter incidental thereto, as may be appropriate in the interests of investors in securities and the securities market.

The power to issue directions under this section shall include and always be deemed to have been included the power to direct any person, who made profit or averted loss by indulging in any transaction or activity in contravention of the provisions of this Act or regulations made thereunder, to disgorge an amount equivalent to the wrongful gain made or loss averted by such contravention.

INVESTIGATIONS PROCEDURE

Section 11C of the Act provides that where SEBI has reasonable ground to believe that the transactions in securities are being dealt with in a manner detrimental to the investors or the securities market; or any intermediary or any person associated with the securities market has violated any of the provisions of this Act or the rules or the regulations made or directions issued by SEBI thereunder, it may, at any time by order in writing, direct any person specified in the order to investigate the affairs of such intermediary or persons associated with the securities market and to report thereon to SEBI.

It is the duty of every manager, managing director, officer and other employee of the company and every intermediary or every person associated with the securities market to preserve and to produce to the Investigating Authority or any person authorised by it in this behalf, all the books, registers, other documents and record of, or relating to the company or, as the case may be, of or relating to the intermediary or such person, which are in their custody or power.

The Investigating Authority may require any intermediary or any person associated with securities market in any manner to furnish such information to, or produce such books, or registers, or other documents, or record before it or any person authorized by it in this behalf as it may consider necessary if the furnishing of such information or the production of such books, or registers, or other documents, or record is relevant or necessary for the purposes of its investigation. The Investigating Authority may keep in its custody any books, registers, other documents and record produced for six months and thereafter shall return the same to any intermediary or any person associated with securities market by whom or on whose behalf the books, registers, other documents and record are produced.

The Investigating Authority may call for any book, or register, other document and record if they are needed again.

Further, if the person on whose behalf the books, registers, other documents and record are produced requires certified copies of the books, registers, other documents and record produced before the Investigating Authority, it shall give certified copies of such books, registers, other documents and record to such person or on whose behalf the books, registers, other documents and record were produced.

Any person, directed to make an investigation may, examine on oath, any manager, managing director, officer and other employee of any intermediary or any person associated with securities market in any manner, in relation to the affairs of his business and may administer an oath accordingly and for that purpose may require any of those persons to appear before it personally.

If any person fails without reasonable cause or refuses to produce to the Investigating Authority or any person authorised by it in this behalf any book, register, other document and record which is his duty to produce; or to furnish any information which it is his duty to furnish; or to appear before the Investigating Authority personally when required to do so or to answer any question which is put to him by the Investigating Authority; or to sign the notes of any examination, he shall be punishable with imprisonment for a term which may extend to one year, or with fine, which may extend to one crore rupees, or with both, and also with a further fine which may extend to five lakh rupees for every day after the first during which the failure or refusal continues.

Sub-section 7 lays down that notes of any examination shall be taken down in writing and shall be read over to, or by, and signed by, the person examined, and may thereafter be used in evidence against him.

Sub-section 8 lays down that where in the course of an investigation, the Investigating Authority has reasonable ground to believe that the books, registers, other documents and record of, or relating to any, any intermediary or any person associated with securities market in any manner may be destroyed, mutilated, altered, falsified or secreted, the Investigating Authority may make an application to the Magistrate or Judge of such during noted court in Mumbai, as may be notified by the Central Government for an order for the seizure of such books, registers, other documents and records.

Sub-section 8A stipulates that the authorised officer may requisition the services of any police officer or any

office of the Central Government, or of both, to assist him for all or any of the purposes specified above and it shall be the duty of every such officer to comply with such requisition.

Sub-section (9) provides that after considering the application and hearing the Investigating Authority, if necessary, the Magistrate or Judge of the Designed Court, by order, authorize the investigating authority –

- (a) to enter, with such assistance, as may be required, the place or places where such books, registers, other documents and record are kept.
- (b) to search that place or those places in the manner specified in the order and.
- (c) to seize books, registers and other documents and records, it consider necessary for the purpose of the investigation.

However, the Magistrate or Judge of the Designated Court shall not authorize seizure of books, registers, other documents and record of any listed public company or a public company (not being the intermediary specified under section 12) which intends to get its securities listed on any recognized stock exchange unless such company indulges in insider trading or market manipulation.

Sub-section 10 provides that the Investigating Authority shall keep in its custody the books, registers, other documents and record seized under this section for such period not later than the conclusion of the investigation as it considers necessary and thereafter shall return the same to the company or the other body corporate, or, as the case may be, to the managing director or the manager or any other person, from whose custody or power they were seized. The Investigating Authority may, before returning such books, registers, other documents and record as aforesaid, place identification marks on them or any part thereof. Every search or seizure made under this section shall be carried out in accordance with the provisions of the Code of Criminal Procedure, 1973 relating to searches or seizures made under that Code.

CEASE AND DESIST PROCEEDINGS

Section 11D deals with the cease and desist powers of SEBI. If SEBI finds, after causing an inquiry to be made, that any person has violated, or is likely to violate any provisions of this Act, or any rules or regulations made thereunder, it may pass an order requiring such person to cease and desist from committing or causing such violation. SEBI shall not pass such order in respect of any listed public company or a public company which intends to get its securities listed on any recognized stock exchange unless SEBI has reasonable grounds to believe that such company has indulged in insider trading or market manipulation.

REGISTRATION OF INTERMEDIARIES

Chapter V of the Act provides for registration of various intermediaries such as stock broker, sub-broker, share transfer agents etc.

Section 12(1) of the Act provides that no stock-broker, sub-broker, share transfer agent, banker to an issue, trustee of trust deed, registrar to an issue, merchant banker, underwriter, portfolio manager, investment adviser and such other intermediary who may be associated with securities market shall buy, sell or deal in securities except under, and in accordance with, the conditions of a certificate of registration obtained from SEBI in accordance with the regulations made under this Act.

A person buying or selling securities or otherwise dealing with the securities market as a stock-broker, sub-broker, share transfer agent, banker to an issue, trustee of trust deed, registrar to an issue, merchant banker, underwriter, portfolio manager, investment adviser and such other intermediary who may be associated with securities market immediately before the establishment of SEBI for which no registration certificate was necessary prior to such establishment, may continue to do so for a period of three months from such establishment or, if he has made an application for such registration within the said period of three months, till the disposal of such application.

Also no depository participant, custodian of securities, foreign institutional investor, credit rating agency or any other intermediary associated with the securities market as SEBI may by notification in this behalf specify, shall buy or sell or deal in securities except under and in accordance with the conditions of a certificate of registration obtained from SEBI in accordance with the regulations made under this Act.

No person shall sponsor or cause to be sponsored or carry on or cause to be carried on any venture capital funds or collective investment schemes including mutual funds, unless he obtains a certificate of registration from SEBI in accordance with the regulations.

It is clarified by SEBI that a collective investment scheme or mutual fund shall not include any unit linked insurance policy or scrips or any such instrument or unit, by whatever name called, which provides a component of investment besides the component of insurance issued by the insurer.

Every application for registration would in such manner and on payment of such fees as may be determined by regulations. SEBI may, by order, suspend or cancel a certificate of registration in such manner as may be determined by regulations. However no such order shall be made unless the person concerned has been given a reasonable opportunity of being heard.

PROHIBITION OF MANIPULATIVE AND DECEPTIVE DEVICES, INSIDER TRADING ETC.

Chapter VA of the Act deals with prohibition of manipulative and deceptive devices, insider trading and substantial acquisition of securities or control.

Section 12A of the Act provides that no person shall directly or indirectly:

- (a) use or employ, in connection with the issue, purchase or sale of any securities listed or proposed to be listed on a recognized stock exchange, any manipulative or deceptive device or contrivance in contravention of the provisions of this Act or the rules or the regulations made thereunder;
- (b) employ any device, scheme or artifice to defraud in connection with issue or dealing in securities which are listed or proposed to be listed on a recognized stock exchange;
- (c) engage in any act, practice, course of business which operates or would operate as fraud or deceit upon any person, in connection with the issue, dealing in securities which are listed or proposed to be listed on a recognized stock exchange, in contravention of the provisions of this Act or the rules or the regulations made thereunder;
- (d) engage in insider trading;
- (e) deal in securities while in possession of material or non-public information or communicate such material or non-public information to any other person, in a manner which is in contravention of the provisions of this Act or the rules or the regulations made thereunder;
- (f) acquire control of any company or securities more than the percentage of equity share capital of a company whose securities are listed or proposed to be listed on a recognized stock exchange in contravention of the regulations made under this Act.

FINANCE, ACCOUNTS AND AUDIT OF SEBI

Chapter VI of the Act provides for Finance, Accounts and Audit of SEBI.

Fund

The Central Government may, after due appropriation made by Parliament by law in this behalf, make to SEBI grants of such sums of money as the Central Government may think fit for being utilised for the purposes of this Act. There shall be constituted a fund to be called the Securities and Exchange Board of India General Fund and

there shall be credited thereto all grants, fees and charges received by SEBI under this Act; all sums received by SEBI from such other sources as may be decided upon by the Central Government. The Fund shall be applied for meeting the salaries, allowances and other remuneration of members, officers and other employees of SEBI, expenses of SEBI in the discharge of its functions and expenses on objects and for purposes authorised by this Act.

Accounts and Audit

SEBI shall maintain proper accounts and other relevant records and prepare an annual statement of accounts in such form as may be prescribed by the Central Government in consultation with the Comptroller and Auditor General of India. The accounts of SEBI shall be audited by the Comptroller and Auditor General of India at such intervals as may be specified by him and any expenditure incurred in connection with such audit shall be payable by SEBI to the Comptroller and Auditor General of India. The Comptroller and Auditor General of India and any other person appointed by him in connection with the audit of the accounts of SEBI shall have the same rights and privileges and authority in connection with such audit as the Comptroller and Auditor General generally has in connection with the audit of the Government accounts and, in particular, shall have the right to demand the production of books, accounts, connected vouchers and other documents and papers and to inspect any of the offices of SEBI. The accounts of SEBI as certified by the Comptroller and Auditor General of India or any other person appointed by him in this behalf together with the audit report thereon shall be forwarded annually to the Central Government and that Government shall cause the same to be laid before each House of Parliament.

PENALTIES FOR FAILURES

Chapter VIA of SEBI Act deals with penalties which can be imposed under the Act for various failures, defaults, non-disclosure and other offences.

It may be recalled that Section 11(2)(i) empowers SEBI to call for information and conduct enquiries and audits of the stock exchanges, mutual funds, other persons associated with securities markets, intermediaries and self regulatory organisations in the security market. Also Section 11(ia) of the Act requires calling for information and record from any bank or any other authority or board or corporation established or constituted by or under any central, state or provincial Act in respect of any transaction in securities which is under investigation or inquiry by SEBI.

Penalty for failure to furnish information, return, etc.

Section 15A lays down that if any person who is required under SEBI Act or any rules or regulations made thereunder, he shall be liable to a penalty of one lakh rupees for each day during which such failure continues or one crore rupees whichever is less, if :

- (a) to furnish any document, return or report to SEBI, fails to furnish the same;
- (b) to file any return or furnish any information, books or other documents within the time specified therefor in the regulations, fails to file return or furnish the same within the time specified therefor in the regulations;
- (c) to maintain books of accounts or records, fails to maintain the same.

Penalty for failure by any person to enter into agreement with clients

Section 15B lays down that if any person who is registered as an Intermediary and is required under this Act or any rules or regulations made thereunder, to enter into an agreement with his client, fails to enter into such agreement, he shall be liable to pay a penalty of one lakh rupees for each day during which such failure continues or one crore rupees whichever is less.

Penalty for failure to redress investors' grievances.

Section 15C lays down that if any listed company or any person who is registered as an Intermediary, after having been called upon by SEBI in writing to redress the grievances of investor, fails to redress such grievances within the time specified by SEBI, such company or intermediary shall be liable to pay a penalty of one lakh rupees for each day during which such failure continues or one crore rupees whichever is less.

Penalties for Default

Section 15D and 15F provide for penalties for default in case of mutual funds :

Section 15D lays down that in case of mutual funds, if any person who is:

- (a) required under this Act or any rules or regulations made thereunder to obtain a certificate of registration from SEBI for sponsoring or carrying on any collective investment scheme, including mutual funds, sponsors or carries on any collective investment scheme, including mutual funds, without obtaining such certificate of registration, he shall be liable to a penalty of one lakh rupees for each day during which he sponsors or carries on any such collective investment scheme, including mutual funds, subject to a maximum of one crore rupees;
- (b) registered with SEBI as a collective investment scheme, including mutual funds, for sponsoring or carrying on any investment scheme, fails to comply with the terms and conditions of certificate of registration, he shall be liable to a penalty which shall not be less than one lakh rupees but which may extend to one lakh rupees for each day during which such failure continues subject to a maximum of one crore rupees;
- (c) registered with SEBI as a collective investment scheme, including mutual funds, fails to make an application for listing of its schemes as provided for in the regulations governing such listing, he shall be liable to penalty which shall not be less than one lakh rupees but which may extend to one lakh rupees for each day during which such failure continues subject to a maximum of one crore rupees;
- (d) registered as a collective investment scheme, including mutual funds, fails to dispatch unit certificates of any scheme in the manner provided in the regulation governing such despatch, he shall be liable to a penalty which shall not be less than one lakh rupees but which may extend to one lakh rupees for each day during which such failure continues subject to a maximum of one crore rupees;
- (e) registered as a collective investment scheme, including mutual funds, fails to refund the application monies paid by the investors within the period specified in the regulations, he shall be liable to a penalty which shall not be less than one lakh rupees but which may extend to one lakh rupees for each day during which such failure continues subject to a maximum of one crore rupees;
- (f) registered as a collective investment scheme, including mutual funds, fails to invest money collected by such collective investment schemes in the manner or within the period specified in the regulations, he shall be liable to a penalty which shall not be less than one lakh rupees but which may extend one lakh rupees for each day during which such failure continues subject to a maximum of one crore rupees.

Penalty for failure to observe rules and regulations by an asset management company

Section 15E lays down that where any asset management company of a mutual fund registered under SEBI Act fails to comply with any of the regulation providing for restrictions on the activities of such company, it shall be liable to a penalty which shall not be less than one lakh rupees but which may extend one lakh rupees for each day during which such failure continues subject to a maximum of one crore rupees.

Penalties for default in case of stock brokers

Section 15F provides if any person registered as a stock broker under SEBI Act -

- (a) fails to issue contract notes in the form and in the manner specified by the stock exchange of which such broker is a member, he shall be liable to a penalty not exceeding five times the amount for which the contract note was required to be issued by that broker;
- (b) fails to deliver any security or fails to make payment of the amount due to the investor in the manner within the period specified in the regulations, he shall be liable to a penalty of one lakh rupees for each day during which such failure continues or one crore rupees, whichever is less;
- (c) charges an amount of brokerage which is in excess of the brokerage specified in the regulations, he shall be liable to a penalty which shall not be less than one lakh rupees but which may extend to five times the amount of brokerage charged in excess of the specified brokerage, whichever is higher.

Penalty for Insider Trading

Section 15G lays down that if any insider:

- (i) either on his own behalf or on behalf of any other person, deals in securities of a body corporate listed on any stock exchange on the basis of any unpublished price sensitive information; or
- (ii) communicates any unpublished price sensitive information to any person, with or without his request for such information except as required in the ordinary course of business or under any law; or
- (iii) counsels, or procures for any other person to deal in any securities of any body corporate on the basis of unpublished price sensitive information,

he shall be liable to a penalty which shall not be less than ten lakh rupees but which may extend to twenty five crore rupees or three times the amount of profits made out of insider trading, whichever is higher.

Penalty for Non-Disclosure of Acquisition of Shares and Takeovers

Section 15H lays down that if any person fails to:

- (i) disclose the aggregate of his shareholding in the body corporate before he acquires any shares of that body corporate; or
- (ii) make such a public announcement to acquire shares at a minimum price; or
- (iii) make a public offer by sending letter of offer to the shareholders of the concerned company; or
- (iv) make payment of consideration to the shareholders who sold their shares pursuant to Letter of offer.

he shall be liable to a penalty which shall not be less than ten lakh rupees but which may extend to twenty five crore rupees or three times the amount of profits made out of such failure, whichever is higher.

Penalty for fraudulent and unfair trade practices

Section 15HA provides that If any person indulges in fraudulent and unfair trade practices relating to securities, he shall be liable to a penalty which shall not be less than five lakh rupees but which may extend to twenty-five crore rupees or three times the amount of profits made out of such practices, whichever is higher.

Penalty for contravention where no separate penalty has been provided

Section 15HB whoever fails to comply with any provision of this Act, the rules or regulations made or directions issued by SEBI thereunder for which no separate penalty has been provided, shall be liable to a penalty which shall not be less than one lakh rupees but which may extend to one crore rupees.

Adjudications

Section 15-I & J deal with SEBI's power to adjudicate and factors to be taken into account by the adjudicating officer.

- (1) For the purpose of adjudging the penalties for failure, SEBI appoints any of its officers not below the rank of Division Chief to be an adjudicating officer for holding an inquiry in the prescribed manner after giving any person concerned a reasonable opportunity of being heard for the purpose of imposing any penalty.
- (2) While holding an inquiry, the adjudicating officer has powers to summon and enforce the attendance of any person acquainted with the facts and circumstances of the case to give evidence or to produce any document which in the opinion of the adjudicating officer, may be useful for or relevant to the subject matter of the inquiry and if, on such inquiry, he is satisfied that the person has failed to comply with the provisions, he may impose such penalty as he thinks fit in accordance with the provisions of any of those sections.
- (3) SEBI may call for and examine the record of any proceedings under this section and if it considers that the order passed by the adjudicating officer is erroneous to the extent it is not in the interests of the securities market, it may, after making or causing to be made such inquiry as it deems necessary, pass an order enhancing the quantum of penalty, if the circumstances of the case so justify.

However, no such order shall be passed unless the person concerned has been given an opportunity of being heard in the matter. Further, nothing contained in this shall not be applicable after an expiry of a period of three months from the date of the order passed by the adjudicating officer or disposal of the appeal under section 15T, whichever is earlier.

Factors to be taken into account by the adjudicating officer

Section 15J lays down that while adjudging the amount of penalty, the adjudicating officer shall have due regard to the following factors viz.,

- (a) the amount of disproportionate gain or unfair advantage, wherever quantifiable, made as a result of the default;
- (b) the amount of loss caused to an investor or group of investors as a result of the default;
- (c) the repetitive nature of the default.

Section 15JA provides that all sums realised by way of penalties under this Act shall be credited to the consolidated fund of India.

Settlement of administrative and civil procedure

Section 15JB deals with settlement of administrative and civil proceeding by SEBI. Any person against where any proceedings have been initiated or may be initiated under section 11, Section 11B, section 11D, section 12(3) or section 15-I, may file an application in writing to SEBI proposing for settlement of proceeding initiated or to be initiated for the alleged defaults. SEBI, may, after taking into consideration the nature, gravity and impact of defaults, agree to the proposal for settlement, on payment of such sum by the defaulter or on such other terms as may be determined by SEBI in accordance with the regulations made under this Act.

The settlement proceedings shall be conducted in accordance with the procedure specified in the regulations made under this Act.

No appeal shall lie under section 15T against any order passed by SEBI or adjudicating officer as the case may be.

SECURITIES APPELLATE TRIBUNAL (SAT)

In order to afford proper appellate remedies, Chapter VIB of SEBI Act provides for the establishment of the Securities Appellate Tribunals to consider appeals against SEBI's orders, of penalties.

As per Section 15K, the Central Government is empowered to establish by notifications one or more Appellate Tribunals, to be known as the Securities Appellate Tribunals to exercise the jurisdiction, power and authorities conferred on such Tribunal by SEBI Act or under the Act or any other law for the time being in force. The Central Government has set up a Tribunal at Mumbai.

Composition of SAT

According to Section 15L, which deals with the composition of the Tribunal, the Securities Appellate Tribunals shall consist of a Presiding Officer and two other members to be appointed by the Central Government by notification.

Qualification for Appointment as Presiding Officer or Member

Section 15M prescribes that a person shall not be qualified for appointment as the Presiding Officer of Securities Appellate Tribunals unless he is a sitting or retired Judge of the Supreme Court or a sitting or retired Chief Justice of a High Court or is a sitting or retired Judge of a High Court who has completed not less than seven years of service as a Judge in a High Court. It has also been prescribed that the presiding officer of the Securities Appellate Tribunal shall be appointed by the Central Government in consultation with chief justice of India or his nominee. A person shall not be qualified for appointment as a member of Securities Appellate Tribunal unless he is a person of ability, integrity and standing who has shown capacity in dealing with problems relating to securities market and has qualification and experience of corporate law, securities laws, finance, economics or accountancy.

A member of SEBI or any person holding a post at senior management level at SEBI cannot be appointed as presiding officer or member of Securities Appellate Tribunal during his service or tenure as such with SEBI or within two years from the date on which he ceases to hold office as such in SEBI.

Tenure of Officer of Presiding Officer and Other Members

Section 15N lays down that the Presiding Officer and every other member of Securities Appellate Tribunal shall hold office for a term of five years from the date he enters upon his office and is eligible for reappointment.

It has also been provided that the person attaining the age of sixty eight years cannot hold office as the presiding officer of Securities Appellate Tribunal. Also a person who has attained the age of sixty two years cannot hold office as member of Securities Appellate Tribunal.

Orders Constituting Appellate Tribunal to be Final and not to Invalidate its Proceedings

Section 15R makes it clear that no order of the Central Government appointing any person as the Presiding Officer or a member of a Securities Appellate Tribunal shall be called in question in any manner, and no Act or proceeding before a Securities Appellate Tribunals shall be called in question in any manner on the ground merely of any defect in the constitution of a Securities Appellate Tribunal.

Requirements for Appeal to the Tribunal

Section 15T and 15U deal with the appeal procedure and power of Securities Appellate Tribunals. Section 15T lays down that any person aggrieved:

- (1) (a) by an order of SEBI made, under this Act, or the rules or regulations made thereunder; or
- (b) by an order made by an adjudicating officer under this Act may prefer an appeal to a Securities Appellate Tribunal having jurisdiction in the matter.

(2) Every appeal shall be filed within a period of 45 days from the date on which a copy of the order made by SEBI or the Adjudicating Officer, as the case may be, is received by him and it shall be in such form and be accompanied by prescribed fee.

However, the Securities Appellate Tribunal may entertain an appeal after the expiry of the said period of 45 days if it is satisfied that there was sufficient cause for not filing it within that period.

(3) On receipt of an appeal, the Securities Appellate Tribunal may, after giving the parties to the appeal, an opportunity of being heard, pass such orders thereon as it thinks fit, confirming, modifying or setting aside the order appealed against.

(4) The Securities Appellate Tribunal shall send a copy of every order made by it to SEBI and the parties to the appeal and to the concerned Adjudicating Officer.

(5) The appeal filed before the Securities Appellate Tribunal shall be dealt with by it as expeditiously as possible and endeavour shall be made by it to dispose of the appeal finally within six months from the date of receipt of the appeal.

PROCEDURE OF SECURITIES APPELLATE TRIBUNAL

As regards the procedure and powers of Securities Appellate Tribunal, Section 15U lays down that the Securities Appellate Tribunal shall not be bound by the procedure laid down by the Code of Civil Procedure, 1908, but shall be guided by the principles of natural justice and, subject to the other provisions of this Act and of any rules, the Securities Appellate Tribunal shall have powers to regulate their own procedure including the places at which they shall have their sittings.

POWERS OF SECURITIES APPELLATE TRIBUNAL

The Securities Appellate Tribunals shall have, for the purposes of discharging their functions under this Act, the same powers as are vested in a Civil Court under the Code of Civil Procedure, 1908, while trying a suit, in respect of the following matters, namely:

- (a) summoning and enforcing the attendance of any person and examining him on oath;
- (b) requiring the discovery and production of documents;
- (c) receiving evidence on affidavits;
- (d) issuing commissions for the examination of witnesses or documents;
- (e) reviewing its decisions;
- (f) dismissing an application for default or deciding it *ex parte*;
- (g) setting aside any order of dismissal of any application for default or any order passed by it *ex parte*; and
- (h) any other matter which may be prescribed.

Every proceeding before the Securities Appellate Tribunal shall be deemed to be a judicial proceeding within the meaning of sections 193 and 228, and for the purposes of section 196 of the Indian Penal Code and the Securities Appellate Tribunal shall be deemed to be a civil court for all the purposes of section 195 and Chapter XXVI of the Code of Criminal Procedure, 1973.

Legal representation

Section 15V permits the appellant either to appear in person or authorise one or more Practising Company Secretaries or Chartered Accountants or Cost Accountants or Legal practitioners or any of its officers to present his or its case before the Securities Appellate Tribunal.

Limitation

As per the section 15W, the provisions of the Limitations Act, 1963 shall apply to an appeal made to Securities Appellate Tribunal.

Public Servants

As per section 15X, the Presiding Officer and other officers and employees of Securities Appellate Tribunal shall be deemed to be public servants within the meaning of Section 21 of the Indian Penal Code.

JURISDICTION OF CIVIL COURT

Section 15Y lays down that no civil court has jurisdiction to entertain any suit or proceeding in respect of any matter which an Adjudicating Officer appointed under this Act or a Securities Appellate Tribunal under this Act is empowered by or under this Act to determine and no injunction shall be granted by any court or other authority in respect of any action taken or to be taken in pursuance of any power conferred by or under this Act.

APPEAL TO SUPREME COURT

Section 15Z lays down that any person aggrieved by any decision or order of the Securities Appellate Tribunal may file an appeal to the Supreme Court within 60 days from the date of communication of the decision or order of the Securities Appellate Tribunal to him on any question of fact or law arising out of such order;

It has been provided that the Supreme Court may, if it is satisfied that the applicant was prevented by sufficient cause from filing the appeal within the said period, allow it to be filed within a further period not exceeding 60 days.

What is the time period for filing an appeal with SAT and Supreme Court?

- In case of filing appeal with SAT: Within 45 days from the date of order of the copy made by SEBI or adjudicating officer.
- In case of filing appeal with Supreme Court: Within 60 days from the date of communication of the decision or order of SAT.

POWERS OF CENTRAL GOVERNMENT***(a) To issue directions***

Section 16 empowers Central Government to issue directions in writing to SEBI on questions of policy as it may deem fit from time to time. However, the Central Government shall as far as practicable, give an opportunity to SEBI to express its views before any such directions is given by the Central Government. The decision of the Central Government as to whether a question is one of policy or not shall be final.

(b) To Supersede SEBI

Section 17 lays down that if at any time the Central Government is of opinion that:

- (a) on account of grave emergency, SEBI is unable to discharge the functions and duties imposed on it by or under the provisions of this Act; or
- (b) SEBI has persistently made default in complying with any direction issued by the Central Government under this Act or in the discharge of the functions and duties imposed on it by or under the provisions of this Act and as a result of such default the financial position of SEBI or the administration of SEBI has deteriorated; or
- (c) circumstances exist which render it necessary in the public interest so to do,

it may, by notification, supersede SEBI for such period, not exceeding six months, as may be specified in the notification.

Upon the publication of the notification, it will have the following effects:

- (a) all the members shall, as from the date of supersession, vacate their offices as such;
- (b) all the powers, functions and duties which may, by or under the provisions of this Act, be exercised or discharged by or on behalf of SEBI, shall until SEBI is reconstituted under sub-section (3), be exercised and discharged by such person or persons as the Central Government may direct; and
- (c) all property owned or controlled by SEBI shall, until SEBI is reconstituted, vest in the Central Government.

On the expiration of the period of supersession specified in the notification, the Central Government may reconstitute SEBI by a fresh appointment and in such case any person or persons who vacated their offices because of supersession shall not be deemed disqualified for appointment.

However, the Central Government may, at any time, before the expiration of the period of supersession, take action. The Central Government shall cause a notification issued and a full report of any action taken under this section and the circumstances to such action to be laid before each House of Parliament at the earliest.

Returns and Reports

As per Section 18, SEBI is required to furnish to the Central Government at such time and in such form and manner as may be prescribed or as the Central Government may direct, such returns and statements and such particulars in regard to any proposed or existing programme for the promotion and development of the securities market, as the Central Government may from time to time require.

SEBI shall within ninety days after the end of each financial year submit to the Central Government a report in such form, as may be prescribed, giving a true and full account of its activities, policy and programmes during the previous financial year and a copy of the report, as soon as may be after it is received, shall be laid down before each House of Parliament.

Delegation of Powers

In accordance with Section 19 of SEBI Act, SEBI may, by general or special order in writing delegate to any member, officer of SEBI or any other person subject to such conditions, if any as may be specified in the order, such of its powers and functions under the Act as it may deem necessary.

Appeal to the Central Government

Section 20 of the Act provides that any person aggrieved by an order of SEBI made under this Act or the rules or regulations made thereunder, may prefer an appeal to the Central Government within such time as may be prescribed. The appeal shall not be admitted if it is preferred after the expiry of the period prescribed therefor. However, if the appellant satisfies the Central Government that he had sufficient cause for not preferring the appeal within the prescribed period.

Every appeal made under this section shall be made in prescribed form and shall be accompanied by a copy of the order appealed against by such fees as may be prescribed.

The procedure for disposing of an appeal shall be such as may be prescribed and the appellant shall be given a reasonable opportunity of being heard.

Bar of Jurisdiction

Section 20A lays down that no order passed by SEBI or the adjudicating officer under this Act shall be appealable except as provided in section 15T or section 20 and no civil court shall have jurisdiction in respect of any matter which SEBI (or the adjudicating officer) is empowered by, or under, this Act to pass any order and no injunction shall be granted by any court or other authority in respect of any action taken or to be taken in pursuance of any order passed by SEBI or the adjudicating officer by, or under, SEBI Act.

Public Servants

Section 22 of the Act provides that all members, officers and other employees of SEBI while acting or purporting to act in pursuance of any of the provisions of the Act shall be deemed to be public servants within the meaning of Section 21 of the Indian Penal Code.

Offences and Punishments

Section 24 lays down that:

- (1) Without prejudice to any award of penalty by the Adjudicating Officer under SEBI Act, if any person contravenes or attempts to contravene or abets the contravention of the provisions of this Act or of any rules or regulations made thereunder, he shall be punishable with imprisonment for a term which may extend to ten years or with fine which may extend to twenty five crore rupees or with both.
- (2) If any person fails to pay the penalty imposed by the Adjudicating Officer or fails to comply with any of his directions or orders, he shall be punishable with imprisonment for a term which shall not be less than one month but which may extend to ten years or with fine which may extend to twenty-five crore rupees or with both.

Section 24A provides any offence punishable under this Act, not being an offence punishable with imprisonment only or with imprisonment and also with fine, may before or after the institutions of any proceeding, be compounded by a Securities Appellate Tribunal or a Court before which such proceedings are pending.

Power to grant Immunity

As per Section 24B of the Act, the Central Government may on the recommendations by SEBI, if satisfied that any person who is alleged to have violated any of the provisions of this Act or the rules or regulations made thereunder has made a full and true disclosures in respect of alleged violations, grant to such persons, subject to conditions as it may think fit, immunity from prosecution for any offence under this Act with respect to the alleged violation.

However, no such immunity shall be granted by the Central Government in cases where the proceedings for the prosecution for any such offence have been instituted before the date of receipt of application for grant of such immunity. It has also been provided that recommendations of SEBI shall not be binding upon the Central Government. However, an immunity granted to a person can be withdrawn by the Central Government, if it is satisfied such person had, in the course of the proceedings not complied with the condition on which the immunity was granted or had given false evidence. Such person may be tried for the offence with respect to which the immunity was granted or for any other offence of which he appears to have been guilty in connection with the contravention. He shall also become liable to the imposition of any penalty under this Act to which such person would have been liable had not such immunity been granted.

Cognizance of Offences by Courts

Section 26 lays down that:

- (1) No court shall take cognizance of any offence punishable under this Act or any rules or regulations made thereunder, save on a complaint made by SEBI.

Establishment of Special Courts

Section 26A empowered the Central Government for providing speedy trial of offences under this Act, by notification, establish or designate as many Special Courts as may be necessary.

A Special Court shall consist of a single judge who shall be appointed by the Central Government with the concurrence of the Chief Justice of the High Court within whose jurisdiction the judge to be appointed is working.

A person shall not be qualified for appointment as a judge of a Special Court unless he is, immediately before such appointment, holding the office of a Sessions Judge or an Additional Sessions Judge, as the case may be.

Offences triable by Special Courts

Section 26B narrates that notwithstanding anything contained in the Code of Criminal Procedure, 1973, all offences under this Act, shall be taken cognizance of and triable by the Special Court established for the area in which the offence is committed or where there are more Special Courts than one for such area, by such one of them as may be specified in this behalf by the High Court concerned.

Application of Code to proceedings before Special Court

Section 26D (1) provides that the provisions of the Code of Criminal Procedure, 1973 shall apply to the proceedings before a Special Court and for the purposes of the said provisions, the Special Court shall be deemed to be a Court of Session and the person conducting prosecution before a Special Court shall be deemed to be a Public Prosecutor within the meaning of clause (u) of section 2 of the Code of Criminal Procedure, 1973.

The person conducting prosecution referred to in sub-section (1) should have been in practice as an Advocate for not less than seven years or should have held a post, for a period of not less than seven years, under the Union or a State requiring special knowledge of law.[26(2)]

Transitional provisions

Section 26E provides that any offence committed under this Act, which is triable by a Special Court shall, until a Special Court is established, be taken cognizance of and tried by a Court of Session exercising jurisdiction over the area, notwithstanding anything contained in the Code of Criminal Procedure, 1973. However, nothing contained in this section shall affect the powers of the High Court, under section 407 of the Code of Criminal Procedure, 1973 to transfer any case or class of cases taken cognizance by a Court of Session under this section.

Offences by Companies

Section 27 on offences by company lays down that:

- (1) Where an offence under this Act has been committed by a company, every person who at the time the offence was committed was in charge of, and was responsible to, the company for the conduct of the business of the company, as well as the company, shall be deemed to be guilty of the offence and shall be liable to be proceeded against and punished accordingly;

However, nothing contained in this sub-section shall render any such person liable to any punishment provided in this Act, if he proves that the offence was committed without his knowledge or that he had exercised all due diligence to prevent the commission of such offence.

- (2) Notwithstanding anything contained in above, where an offence under this Act has been committed by a company and it is proved that the offence has been committed with the consent or connivance of, or is attributable to any neglect on the part of, any director, manager, secretary or other officer of the company, such director, manager, secretary or other officer shall also be deemed to be guilty of the offence and shall be liable to be proceeded against and punished accordingly.

Recovery of amounts

Section 28A(1) provides that if a person fails to pay the penalty imposed by the adjudicating officer or fails to comply with any direction of SEBI for refund of monies or fails to comply with a direction of disgorgement order issued under section 11B or fails to pay any fees due to SEBI, the Recovery Officer may draw up under his signature a statement in the specified form specifying the amount due from the person (such statement being

hereafter in this Chapter referred to as certificate) and shall proceed to recover from such person the amount specified in the certificate by one or more of the following modes, namely:-

- (a) attachment and sale of the person's movable property;
- (b) attachment of the person's bank accounts;
- (c) attachment and sale of the person's immovable property;
- (d) arrest of the person and his detention in prison;
- (e) appointing a receiver for the management of the person's movable and immovable properties,

and for this purpose, the provisions of section 220 to 227, 228A, 229, 232, the Second and Third Schedules to the Income-tax Act, 1961 and the Income-tax (Certificate Proceedings) Rules, 1962, as in force from time to time, in so far as may be, apply with necessary modifications as if the said provisions and the rules made thereunder were the provisions of this Act and referred to the amount due under this Act instead of to income-tax under the Income-tax Act, 1961.

Explanation 1- For the purpose of this sub-section, the person's movable or immovable property or monies held in bank accounts shall include any property or monies held in bank accounts which has been transferred directly or indirectly on or after the date when the amount specified in certificate had become due, by the person to his spouse or minor child or son's wife or son's minor child, otherwise than for adequate consideration, and which is held by, or stands in the name of, any of the persons aforesaid; and so far as the movable or immovable property or monies held in bank accounts so transferred to his minor child or his son's minor child is concerned, it shall, even after the date of attainment of majority by such minor child or son's minor child, as the case may be, continue to be included in the person's movable or immovable property or monies held in bank accounts for recovering any amount due from the person.

Explanation 2- Any reference under the provisions of the Second and Third Schedules to the Income-tax Act, 1961 and the Income-tax (Certificate Proceedings) Rules, 1962 to the assessee shall be construed as a reference to the person specified in the certificate.

Explanation 3- Any reference to appeal in Chapter XVIII and the Second Schedule to the Income-tax Act, 1961, shall be construed as a reference to appeal before the Securities Appellate Tribunal under Section 15T of this Act.

"Recovery Officer" means any officer of SEBI who may be authorized, by general or special order in writing, to exercise the powers of a Recovery Officer.

Sub-section (2) empowered the Recovery Officer to seek the assistance of the local district administration while exercising the powers.

The recovery of amounts by a Recovery Officer, pursuant to non compliance with any direction issued by SEBI under section 11B, shall have precedence over any other claim against such person.

Power to make Rules

Section 29 empowers the Central Government to make rules for carrying out the purposes of this Act.

Power of SEBI to make Regulations

Section 30 empowers SEBI by notification to make regulations consistent with this Act and the rules made thereunder to carry out the purposes of this Act.

Such regulations may provide for all or any of the following matters, namely:

- (a) the times and places of meetings of SEBI and the procedure to be followed at such meetings including quorum necessary for the transaction of business;

- (b) the terms and other conditions of service of officers and employees of SEBI;
- (c) the matters relating to issue of capital, transfer of securities and other matters incidental thereto and the manner in which such matters shall be disclosed by the companies under section 11A.
- (ca) the utilisation of the amount credited under sub-section 5 of section 11;
- (cb) the fulfillment of other conditions relating to Collective Investment scheme under sub-section (2A) of section 11AA;
- (cc) the procedure to be followed by the authorized officer for search or seizure under sub-section (9) of section 11C;
- (d) the conditions subject to which certificate of registration is to be issued, the amount of fee to be paid for certificate of registration and the manner of suspension or cancellation of certificate of registration.
- (da) the terms determined by SEBI for settlement of proceedings under sub-section (2) and the procedure for conducting of settlement proceedings under sub-section (3) of section 15JB.
- (db) any other matter which is required to be, or may be, specified by regulation or in respect of which provision is to be made by regulations.

Rules, Regulations to be laid before the Parliament

Section 31 lays down that every rule and every regulation made under this Act shall be laid, as soon as may be after it is made, before each House of Parliament, while it is in session, for a total period of thirty days which may be comprised in one session or in two or more successive sessions, and if, before the expiry of the session immediately following the session or the successive sessions aforesaid, both Houses agree in making any modification in the rule or regulation or both Houses agree that the rule or regulation should not be made, the rule or regulation shall thereafter have effect only in such modified form or be of no effect, as the case may be; so, however, that any such modification or annulment shall be without prejudice to the validity of anything previously done under that rules or regulation.

Section 32 lays down that the provisions of this Act shall be in addition to, and not in derogation of, the provisions of any other law for the time being in force.

SEBI (SETTLEMENT OF ADMINISTRATIVE & CIVIL PROCEEDINGS) REGULATIONS, 2014

Under the SEBI Act, 1992, Securities Contracts (Regulation) Act, 1956 (SCRA) and the Depositories Act, 1996, SEBI pursues two streams of enforcement actions i.e. Administrative/Civil or Criminal. Administrative/civil actions include issuing directions such as remedial orders, cease and desist orders, suspension or cancellation of certificate of registration and imposition of monetary penalty under the respective statutes and action pursued or defended in a court of law/tribunal. Criminal action involves initiating prosecution proceedings against violators by filing complaint before a criminal court. Consent order is a remedial measure for settling civil proceedings initiated by SEBI.

Consent Order means an order settling administrative or civil proceedings between the regulator and a person (Party) who may prima facie be found to have violated securities laws. Consent Order provides flexibility of wider array of enforcement and remedial actions which will achieve the twin goals of an appropriate sanction, remedy and deterrence without resorting to litigation, lengthy proceedings and consequent delays.

SEBI vide circular ref no. EFD/ED/Cir-1/2007 dated April 20, 2007 laid down the framework for passing of consent orders and for considering requests for composition of offences under SEBI Act, SC(R) Act and Depositories Act. Again in the year 2012 SEBI with the purpose of providing more clarity on its scope and applicability, partially modified the same.

The President of India promulgated the Securities Laws (Amendment) Second Ordinance, 2013 on September 16, 2013 conferring explicit powers on SEBI to settle administrative and civil proceedings under section 15JB of the Securities and Exchange Board of India Act, 1992 (SEBI Act), section 23JA of the Securities Contracts (Regulation) Act, 1956 and section 19-IA of the Depositories Act, 1996.

The said Ordinance provided that SEBI may, after taking into consideration the nature, gravity and impact of defaults, agree to the proposal for settlement, on payment of such sum by the defaulter or on such other terms as may be determined by SEBI in accordance with the regulations made under SEBI Act. The said Ordinance further provided that the settlement proceedings shall be conducted in accordance with the procedure specified in the regulations made under SEBI Act. In this direction SEBI also placed a draft consultation paper on SEBI (Settlement of Administrative and Civil Proceedings) Regulations, 2013 on its website for public comments.

In the light of the above, SEBI framed SEBI (Settlement of Administrative and Civil Proceedings) Regulations, 2014 and notified it vide Circular No. LAD-NRO/GN/2013-14/37/50 dated 09 January, 2014. These regulations will enable the persons who have defaulted on any SEBI laws & civil proceedings have been initiated against them, to settle the proceedings. These regulations do not provide for settling proceedings which are under criminal in nature.

These regulations provide for the involved entity to file settlement plea within 60 days of the show cause notice served to them by SEBI. The charges and related costs would not be considered upon the payment of settlement also in the cases in which the applicant has already been a party to two earlier settlements. The regulation mentions the minimum amount to be paid by entities, which will vary as per the charges against them. These charges will be highest for the promoters.

SEBI (Settlement of Administrative & Civil Proceedings) Regulations, 2014 is divided into VIII chapters and two schedules. Chapter 1 covers the preliminary definitions part. Chapter II deals with the application for settlement and limitations part. Chapter III stipulates the scope of settlement proceedings, withdrawal of application for settlement, effect of pending application on the specified proceedings etc, Chapter V deals with the terms of settlement like monetary and non-monetary terms, factors to be considered to arrive at the settlement terms, Chapter V defined the role of the internal committee and high powered advisory committee in order to impart transparency in the process, Chapter VI provides the procedure of settlement before the internal committee and high powered advisory committee, Chapter VII deals with Settlement orders like settlement of proceeding before the adjudicating officer and SEBI or Settlement proceeding pending before tribunal or any court, Rejection of application in certain eventualities and chapter VIII deals with miscellaneous information like confidentiality of information, power to remove difficulties, SEBI's power to specify procedures, Rescission and savings etc. Schedule I is divided into three parts A, B & C respectively and Schedule II is again divided into seven chapters. The highlights of the regulations in brief is discussed below:

Scope of Settlement Proceeding

Regulation 5 deals with the scope settlement proceedings. It provides that an application for settlement of any specified proceeding shall not be considered, if:

- (a) the alleged default was committed within a period of 24 calendar months from the date of the last settlement order where the applicant was a party.
- (b) An earlier application with regard to the same alleged default has been rejected;

However, such an application may be considered in exceptional circumstances, such as the lapse of time since the commission of the alleged default, the weight of evidence against the applicant, etc. and subject to the payment of such additional fees and/or interest on the settlement amount from the date of rejection of the earlier application till the date of payment of the settlement amount, as may be recommended by the high powered advisory committee.

- (c) the applicant has been party to two settlement orders during the period of thirty six calendar months, prior to the date of applications;

- (d) the audit or investigation, if any, in respect of any alleged default, is not complete.

The following proceedings are out of the scope of these regulations, i.e. a specified proceeding cannot be settled, if it involves any of the following defaults:

- (a) defaults involving insider trading and communication of unpublished price sensitive information ;
- (b) fraudulent and unfair trade practices including front running, which in the opinion of SEBI are serious and have a market wide impact or have caused substantial losses to or affect the rights of investors in securities, especially retail investors and small shareholders:

Explanation.- The expression ' front running' means usage of non-public information to directly or indirectly, buy or sell securities or enter into options or futures contracts, in advance of a substantial order, on an impending transaction, in the same or related securities or futures or options contracts, in anticipation that when the information becomes public; the price of such securities or contracts may change;

- (c) failure to make an open offer except where the applicant agrees to make the open offer or where SEBI is of the opinion that the making of the open offer would not be beneficial to the shareholders or is infructuous;
- (d) defaults or manipulative practices by mutual funds, alternative investment funds, collective investment schemes and their sponsors or asset management companies, collective investment management company, managers, trustees that result in substantial losses to investors, except in cases where the applicant has compensated the investors for the losses, to the satisfaction of SEBI;
- (e) failure to redress investor grievances except where the alleged default is with regard to delayed redressal;
- (f) failure, by issuers of securities or entities who invite investment, to make material disclosures in offer documents;
- (g) raising of monies by issuance of securities or pooling of funds, in violation of securities laws where the remedy is refund of such monies;
- (h) non-compliance of notices and summons issued by SEBI or summons issued by the adjudicating officer;
- (i) non-compliance of any order or direction passed under the securities laws.

So any civil proceedings apart from above can be brought under these regulations & can be settled.

Settlement Terms

Regulation 8 provides for the terms of settlement in monetary as well as non-monetary terms or both. The non-monetary terms may include appropriate directions, such as:

- (a) Voluntary suspension of certificate of registration or closure of business for a specified period;
- (b) Removal from management;
- (c) Direction in the nature of disgorgement, where it is possible to identify the investors who have incurred losses on account of the action or inaction of the applicant;
- (d) Debarment of certain individuals from acting as a partner or officer or director of an intermediary or as an officer or director of a company that has a class of securities regulated by SEBI, for specified periods;
- (e) Cancellation of securities and reduction in share holding where the securities are issued fraudulently including cancellation of bonus shares received on such securities, if any, and re-imbursement of any dividends received, etc;
- (f) Voluntary lock-in of securities;
- (g) Implementation of enhanced policies and procedures to prevent future securities laws violations as well as direction to appoint or retain an independent consultant to review policies and procedures;

- (h) Direction to provide enhanced training and education to employees of intermediaries;
- (i) Directions relating to internal audit and reporting requirements;
- (j) Any other directions that may be issued by SEBI under the securities laws in the interest of the investors.

The amount of settlement will be credited in the Consolidated Fund of India. The application fee, the additional processing fee accompanying the application for condonation of delay and the legal cost will be included in the general fund of SEBI. The ill-gotten profits made (if any) will be credited in SEBI's Investor Protection and Education Fund.

Factors to be considered to arrive at the settlement terms

Regulation 9 deals with the factors to be considered by SEBI while arriving at the settlement terms, including but not limited to the following:

- (a) conduct of the applicant in the investigation;
- (b) the role played by the applicant in case the alleged default is committed by a group of persons;
- (c) nature, gravity and impact of alleged defaults;
- (d) whether any other proceeding against the applicant for non-compliance of securities laws is pending or concluded;
- (e) whether the alleged default is minor or major in nature;
- (f) the extent of amount of harm and/or loss to investors' and/or gain by the applicant;
- (g) processes which have been introduced since the alleged default to minimize future defaults or lapses;
- (h) compliance schedule proposed by the applicant;
- (i) economic benefits accruing to any person from the non-compliance or delayed compliance;
- (j) conditions which are necessary to deter future non-compliance by the same or another person;
- (k) satisfaction of claim of investors regarding payment of money due to them or delivery of securities to them;
- (l) whether the applicant has undergone any other enforcement action for the same violation;
- (m) any other factors necessary in the facts and circumstances of the case.

Procedure

1. The person who wants to have proceedings settled have to make application along with requisite fees.
2. The applicant shall make full & true disclosures.
3. Application should be complete & if not complete it will be returned. The return of application can be resubmitted within 15 days from the day of rejection of application.
4. The Settlement terms include settlement amount &/or non-monetary terms. The settlement amount will be calculated in accordance with the guidelines specified in Schedule II of these regulations.
5. The settlement once completed will be published on SEBI website.
6. If there is any non compliance of settlement order then the original proceedings which was settled would be restored.
7. The application may be rejected if applicant refuses to receive or respond to the communications sent by SEBI or non submission or delays the submission of information, document, etc. as required or non appearance

before the internal committee on more than one occasion or violates in any manner the undertaking and waivers specified, or non remittance or delays the payment of settlement amount and/or does not abide by the undertaking and waivers.

SEBI (PROCEDURE FOR SEARCH AND SEIZURE) REGULATIONS, 2014

Sebi (Procedure for Search and Seizure) Regulations, 2014 is repealed with effect from 17th September, 2015.

LESSON ROUND UP

- SEBI has twin objectives of protecting the interests of the investors and to promote the development of, and to regulate the securities markets by such measures as it thinks fit.
- SEBI regulates the securities market and SAT acts as a watchdog to ensure justice.
- Section 15 Y of the SEBI Act provides that no civil court shall have jurisdiction to entertain a suit or proceeding in respect of any matter in which an adjudicating officer ('AO') is appointed under the Act or SAT is empowered by or under the Act to determine and no injunction shall be granted by any court or other authority in respect of any action taken or to be taken in pursuance of any power conferred by or under the Act.
- SEBI Act, 1992 empowers for appellate remedies against SEBI's order or penalties by establishing Securities Appellate Tribunal.
- Any person aggrieved by any decision or order of the SAT can file an appeal to Supreme Court.
- Appearance before SAT may be either in person or through authorized person being a Chartered Accountant, Company Secretary, Cost Accountant or Legal Practitioner.
- The Central Government may, for the purpose of providing speedy trial of offences under this Act, by notification, established or designate as many special courts as may be necessary.
- SEBI (Settlement of Administrative and Civil Proceedings) Regulations, 2014 is divided into VIII chapters and two schedules.

GLOSSARY

Compounding of offences	Compounding of offence allows the accused to avoid a lengthy process of criminal prosecution, which would save cost, time, mental agony, etc. in return for payment of compounding charges.
Injunction	A court order by which an individual is required to perform, or is restrained from performing, a particular act.
Tribunal	Article 227 of the Constitution of India defines 'tribunal' as a person or a body other than a Court set up by the State for deciding rights of contending parties in accordance with rules framed for regulation having force of law.
SAT	Securities Appellate Tribunal is a quasi-judicial body established by Central Government by notification to exercise the jurisdiction, powers and authority conferred on such Tribunal by or under SEBI Act or any other law for the time being in force.

SELF TEST QUESTIONS

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation.)

1. What are the prime objectives of SEBI?

2. Discuss the various powers and functions of the SEBI.
3. Explain the role of SEBI in strengthening regulatory framework and fostering investor confidence.
4. Enumerate the various penalties which can be imposed under SEBI Act, 1992 for various failures, defaults, non-disclosure and other offences.
5. Explain the procedure for Appeal to the Securities Appellate Tribunal.
6. Discuss the various powers of the Central Government under SEBI Act, 1992.

Lesson 18

Depositories

LESSON OUTLINE

- Introduction
- Benefits of Depository System
- Depository System – An Overview
- Legal Linkage
- Legal Framework
- The Depositories Act, 1996
- Bye-laws of a Depository
- SEBI (Depositories and Participants) Regulations, 1996
- Governance of Depository
- Internal Audit of Depository Participants
- Concurrent Audit
- Establishment of connectivity with NSDL & CDSL
- Appointment of Common Agency for Share Registry Work
- In Person Verification
- Designated Depository Participants
- Basic Services Demat Account
- Single registration for depository participants
- Saral account opening form for resident individuals
- LESSON ROUND UP
- GLOSSARY
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

The inception of depository system in the Indian Capital market has been during the 90's. The depositories are an important intermediaries in the securities market that is scrip-less or moving towards such a state. The erstwhile settlement system on Indian stock exchanges involved movement of paper securities to the issuer for registration, with the change of ownership being evidenced by an endorsement on the security certificate. Theft, forgery, mutilation of certificates and other irregularities provided the issuer right to refuse the transfer of a security. Added costs and delays in settlement, restricted liquidity and made investor grievance redressal time consuming. To obviate these problems, the Depositories Act, 1996 was passed and subsequently the regulations were notified.

This lesson is designed to enable the student to understand the basic concept of depository, depository participants, functions, rights and obligations of depositories, benefits of depositories, dematerialisation process, and the regulatory framework for depository in India.

INTRODUCTION

A Depository is an organization like a Central Bank where the securities of a shareholder are held in the electronic form at the request of the shareholder through the medium of a Depository Participant. To utilize the services offered by a Depository, the investor has to open an account with the Depository through a Depository Participant.

According to Section 2(e) of the Depositories Act, 1996. "Depository means a company formed and registered under the Companies Act, 2013 and which has been granted a certificate of registration under Section 12(1A) of the SEBI Act, 1992".

A depository cannot act as a depository unless it obtains a certificate of commencement of business from SEBI.

There are two Depositories functioning in India, namely the National Securities Depository Limited (NSDL) and the Central Depository Services (India) Limited (CDSL). Under the provisions of the Depositories Act, these Depositories provide various services to investors and other Participants in the capital market, such as, clearing members, stock exchanges, investment institutions, banks and issuing corporates. These include basic facilities like account opening, dematerialization, settlement of trades and advanced facilities like pledging, distribution of non-cash corporate actions, distribution of securities to allottees in case of public issues, etc.

All the securities held by a depository shall be dematerialized and shall be in a fungible form. To utilize the services offered by a depository, the investor has to open an account with the depository through a participant, similar to the opening of an account with any of the bank branches to utilize services of that bank. Registration of the depository is required under SEBI (Depositories and Participants) Regulations, 1996 and is a precondition to the functioning of the depository. Depository and depository participant both are regulated by SEBI.

Difference between Depository and Custodian

Both depository and custodial services are responsible for safe keeping of securities but they are different in the sense that the Depository can legally transfer beneficial ownership, which a custodian cannot. The main objective of a Depository is to minimize the paper work involved with the ownership, trading and transfer of securities.

BENEFITS OF DEPOSITORY SYSTEM

In the depository system, the ownership and transfer of securities takes place by means of electronic book entries. At the outset, this system rids the capital market of the dangers related to handling of paper. The system provides numerous direct and indirect benefits, like:

Elimination of bad deliveries - In the depository environment, once holdings of an investor are dematerialised, the question of bad delivery does not arise i.e. they cannot be held "under objection". In the physical environment, buyer of shares was required to take the risk of transfer and face uncertainty of the quality of assets purchased. In a depository environment good money certainly begets good quality of assets.

Elimination of all risks associated with physical certificates - Dealing in physical securities have associated security risks of theft of stocks, mutilation of certificates, loss of certificates during movements through and from the registrars, thus exposing the investor to the cost of obtaining duplicate certificates and advertisements, etc. This problem does not arise in the depository environment.

Immediate transfer and registration of securities - In the depository environment, once the securities are credited to the investors account on pay out, he becomes the legal owner of the securities. There is no further need to send it to the company's registrar for registration. Having purchased securities in the physical environment, the investor has to send it to the company's registrar so that the change of ownership can be registered. This process usually takes around three to four months and is rarely completed within the statutory framework of two

months thus exposing the investor to opportunity cost of delay in transfer and to risk of loss in transit. To overcome this, the normally accepted practice is to hold the securities in street names i.e. not to register the change of ownership. However, if the investors miss a book closure the securities are not good for delivery and the investor would also stand to lose his corporate entitlements.

Faster disbursement of non cash corporate benefits like rights, bonus, etc. – Depository system provides for direct credit of non cash corporate entitlements to an investor's account, thereby ensuring faster disbursement and avoiding risk of loss of certificates in transit.

Reduction in brokerage by many brokers for trading in dematerialized securities - Brokers provide this benefit to investors as dealing in dematerialized securities reduces their back office cost of handling paper and also eliminates the risk of being the introducing broker.

Reduction in handling of huge volumes of paper and periodic status reports to investors on their holdings and transactions, leading to better controls.

Elimination of problems related to change of address of investor, transmission, etc. - In case of change of address or transmission of demat shares, investors are saved from undergoing the entire change procedure with each company or registrar. Investors have to only inform their DP with all relevant documents and the required changes are effected in the database of all the companies, where the investor is a registered holder of securities.

Elimination of problems related to selling securities on behalf of a minor - A natural guardian is not required to take court approval for selling demat securities on behalf of a minor.

DEPOSITORY SYSTEM - AN OVERVIEW

The Depository System functions very much like the banking system. A bank holds funds in accounts whereas a Depository holds securities in accounts for its clients. A Bank transfers funds between accounts whereas a Depository transfers securities between accounts. In both systems, the transfer of funds or securities happens without the actual handling of funds or securities. Both the Banks and the Depository are accountable for the safe keeping of funds and securities respectively.

In the depository system, share certificates belonging to the investors are to be dematerialized and their names are required to be entered in the records of depository as beneficial owners. Consequent to these changes, the investors' names in the companies' register are replaced by the name of depository as the registered owner of the securities. The depository, however, does not have any voting rights or other economic rights in respect of the shares as a registered owner. The beneficial owner continues to enjoy all the rights and benefits and is subject to all the liabilities in respect of the securities held by a depository. Shares in the depository mode are fungible and cease to have distinctive numbers. The transfer of ownership changes in the depository is done automatically on the basis of delivery vs. payment.

In the Depository mode, corporate actions such as IPOs, rights, conversions, bonus, mergers/amalgamations, subdivisions & consolidations are carried out without the movement of papers, saving both cost & time. Information of beneficiary owners is readily available. The issuer gets information on changes in shareholding pattern on a regular basis, which enables the issuer to efficiently monitor the changes in shareholdings.

The Depository system links the issuing corporates, Depository Participants (DPs), the Depositories and clearing corporation/ clearing house of stock exchanges. This network facilitates holding of securities in the soft form and effects transfers by means of account transfers.

Following presentation about depositories reveal all about depositories, its concepts and trading, i.e. models of depositories, Depository functions, Legal linkage, depository participant, Registrars and issuers, dematerialisation, rematerialisation, electronic credit in new issues, trading system, corporate action.

MODELS OF DEPOSITORY

Immobilisation – Where physical share certificates are kept in vaults with the depository for safe custody. All subsequent transactions in these securities take place in book entry form. The actual owner has the right to withdraw his physical securities as and when desired. The immobilization of fresh issue may be achieved by issuing a jumbo certificate representing the entire issue in the name of depository, as nominee of the beneficial owners.

Dematerialisation – No Physical scrip in existence, only electronic records maintained by depository. This type of system is cost effective and simple and has been adopted in India.

Dematerialization

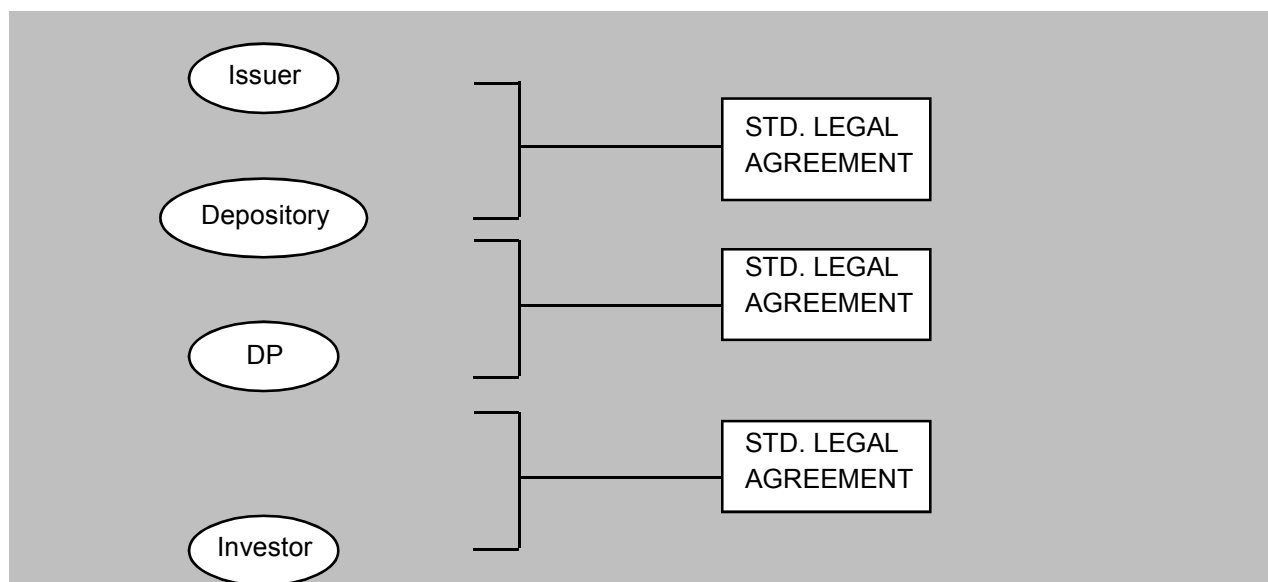
Dematerialization is a process by which the physical share certificates of an investor are taken back by the Company and an equivalent number of securities are credited his account in electronic form at the request of the investor. An investor will have to first open an account with a Depository Participant and then request for the dematerialization of his share certificates through the Depository Participant so that the dematerialized holdings can be credited into that account. This is very similar to opening a Bank Account.

Dematerialization of shares is optional and an investor can still hold shares in physical form. However, he/she has to demat the shares if he/she wishes to sell the same through the Stock Exchanges. Similarly, if an investor purchases shares from the Stock Exchange, he/she will get delivery of the shares in demat form. Odd lot share certificates can also be dematerialized.

Depository Functions

- Account opening
- Dematerialisation
- Rematerialisation
- Settlement
- Initial Public Offers (IPO's), corporate benefits
- Pledging

LEGAL LINKAGE



DEPOSITORY PARTICIPANT

Just as a brokers act an agent of the investor at the Stock Exchange; a Depository Participant (DP) is the representative (agent) of the investor in the depository system providing the link between the Company and investor through the Depository. The Depository Participant maintains securities account balances and intimate the status of holding to the account holder from time to time. According to SEBI guidelines, Financial Institutions like banks, custodians, stockbrokers etc. can become participants in the depository. A DP is one with whom an investor needs to open an account to deal in shares in electronic form. While the Depository can be compared to a Bank, DP is like a branch of that bank with which an account can be opened. The main characteristics of a depository participant are as under:

- Acts as an Agent of Depository
- Customer interface of Depository
- Functions like Securities Bank
- Account opening
- Facilitates dematerialisation
- Instant transfer on pay-out
- Credits to investor in IPO, rights, bonus
- Settles trades in electronic segment

REGISTRAR/ISSUER

- Dematerialisation
- Confirmation of Beneficiary Holdings
- Corporate Actions – Rights, Bonus, etc.
- Reconciliation of Depository Holdings
- Rematerialisation

DEMATERIALISATION

- Investor opens account with DP
- Fills Dematerialisation Request Form (DRF) for registered shares
- Investor lodges DRF and certificates with DP
- DP intimates the Depository
- Depository intimates Registrar/Issuer
- DP sends certificates and DRF to Registrar/Issuer
- Registrar/Issuer confirms demat to Depository
- Depository credits investor a/c

REMATERIALISATION

- Client submits Rematerialisation Request Form (RRF) to DP
- DP intimates Depository
- Depository intimates the Registrar/Issuer

- DP sends RRF to the Registrar/Issuer
- Registrar/Issuer prints certificates and sends to Investor
- Registrar/Issuer confirms remat to Depository
- Investor's account with DP debited

ELECTRONIC CREDIT IN NEW ISSUES

- Investor opens account with DP
- Submits application with option to hold securities in depository giving DP-Id and Client-Id
- Registrar uploads list of allottees to Depository
- Depository credits allottee's account with DP
- Refunds sent by Registrar as usual

TRADING SYSTEM

- Separate quotes in Book Entry
- Trading Member to have Clearing Account with DP
- Settlement as per Settlement Calendar of Stock Exchange
- Trading can be introduced in any Stock exchange if settlement is guaranteed

CORPORATE ACTIONS

- Dividends/cash benefits – these benefits are directly forwarded to the investors by the company or its registrar and transfer agent.
- Non-cash benefits, viz. Bonus, Rights Issue, etc. – these benefits are electronically credited to the beneficial owner's account through Depository.

LEGAL FRAMEWORK

The legal framework for a depository system has been laid down by the Depositories Act, 1996 and is regulated by SEBI. The depository business in India is regulated by –

- The Depositories Act, 1996
- The SEBI (Depositories and Participants) Regulations, 1996
- Bye-laws of Depository
- Business Rules of Depository.

Apart from the above, Depositories are also governed by certain provisions of:

- The Companies Act, 2013
- The Indian Stamp Act, 1899
- Securities and Exchange Board of India Act, 1992
- Securities Contracts (Regulation) Act, 1956
- Benami Transaction (Prohibition) Act, 1988
- Income Tax Act, 1961
- Bankers' Books Evidence Act, 1891

The legal framework for depository system in the Depositories Act, 1996 provides for the establishment of single or multiple depositories. Any body to be eligible for providing depository services must be formed and registered as a company under the Companies Act, 2013 and seek registration with SEBI and obtain a Certificate of Commencement of Business from SEBI on fulfillment of the prescribed conditions. The investors opting to join depository mode are required to enter into an agreement with depository through a participant who acts as an agent of depository. The agencies such as custodians, banks, financial institutions, large corporate brokerage firms, non-banking financial companies etc. act as participants of depositories. The companies issuing securities are also required to enter into an agreement with the Depository.

THE DEPOSITORIES ACT, 1996

OBJECTIVES

The depositories legislation as per the Statement of Objects and Reasons appended to the Depositories Act, 1996 aims at providing for:

- A legal basis for establishment of depositories to conduct the task of maintenance of ownership records of securities and effect changes in ownership records through book entry;
- Dematerialisation of securities in the depositories mode as well as giving option to an investor to choose between holding securities in physical mode and holding securities in a dematerialized form in a depository;
- Making the securities fungible;
- Making the shares, debentures and any interest thereon of a public limited company freely transferable; and
- Exempting all transfers of shares within a depository from stamp duty.

ELIGIBILITY CONDITION FOR DEPOSITORY SERVICES

Any company or other institution to be eligible to provide depository services must:

- be formed and registered as a company under the Companies Act, 2013.
- be registered with SEBI as a depository under SEBI Act, 1992.
- has framed bye-laws with the previous approval of SEBI.
- has one or more participants to render depository services on its behalf.
- has adequate systems and safeguards to prevent manipulation of records and transactions to the satisfaction of SEBI.
- complies with Depositories Act, 1996 and SEBI (Depositories and Participants) Regulations, 1996.
- meets eligibility criteria in terms of constitution, network, etc.

ELIGIBLE SECURITIES REQUIRED TO BE IN THE DEPOSITORY MODE

Section 8 of the Depositories Act gives the option to the investors to receive securities in physical form or in depository mode.

It is not necessary that all eligible securities must be in the depository mode. In the scheme of the Depositories legislation, the investor has been given supremacy. The investor has the choice of holding physical securities or opt for a depository based ownership record.

However, in case of fresh issue of securities all securities issued have to be in dematerialized form. However

after that investor will also have the freedom to switch from depository mode to non-depository mode and vice versa. The decision as to whether or not to hold securities within the depository mode and if in depository mode, which depository or participant, would be entirely with the investor.

FUNGIBILITY

Section 9 states that securities in depositories shall be in fungible form.

The Act envisages that all securities held in depository shall be fungible i.e. all certificates of the same security shall become interchangeable in the sense that investor loses the right to obtain the exact certificate he surrenders at the time of entry into depository. It is like withdrawing money from the bank without bothering about the distinctive numbers of the currencies.

Immobilisation of securities in a depository mode refers to a situation where the depository holds securities in the form of physical paper side by side with electronic evidence of ownership. In such a case the transfers are not accompanied by physical movement of securities but securities are in existence in the custody of the depository. However, the Depositories Act, envisages dematerialisation in the depository mode. In such a case the securities held in a depository shall be dematerialized and the ownership of the securities shall be reflected through book entry only. The securities outside the depository shall be represented by physical scrips. Hence, the depository legislation envisages partial dematerialisation, i.e. a portion of the securities in dematerialized form and the other portion in physical form. (Sections 89 and 186 of Companies Act, 2013 shall not apply to a depository in respect of shares held on behalf of beneficial owners in depositories).

RIGHTS OF DEPOSITORIES AND BENEFICIAL OWNER

A depository should be deemed to be the registered owner for the purposes of effecting transfer of ownership of security on behalf of a beneficial owner. The depository as a registered owner should not have any voting rights or any other rights in respect of securities held by it. The beneficial owner is entitled to all the rights and benefits and be subjected to all the liabilities in respect of his securities held by a depository.

REGISTER OF BENEFICIAL OWNER

Every depository is required to maintain a register and an index of beneficial owners in the manner provided in the Companies Act, 2013.

RECORDING OF NON DISPOSAL UNDERTAKING (NDU) IN THE DEPOSITORY SYSTEM

SEBI has allowed depositories to offer a system for recording of non-disposal undertaking (NDU). In this direction, the depositories are advised the following:

- Depositories shall develop a separate module/ transaction type in their system for recording NDUs.
- Both parties to the NDU shall have a demat account with the same depository and be KYC compliant.
- Pursuant to entering the NDU, the Beneficial Owner (BO) along with the other party shall make an application through the participant (where the BO holds his securities) to the depository, for the purpose of recording the NDU transaction.
- The application shall necessarily include details of BO ID, PAN, email-id, signature(s), name of the entity in whose favour such NDU is entered and the quantity of securities. Such entity in whose favour NDU is entered shall also authorize the participant of the BO holding the shares, to access the signatures as recorded in that entity's demat account.
- The participant after being satisfied that the securities are available for NDU shall record the NDU and freeze for debit the requisite quantity of securities under NDU in the depository system. .
- The depositories shall make suitable provisions for capturing the details of BO ID and PAN of the entity

in whose favour such NDU is entered by the participant. The depositories shall also make available to the said participant, the details of authorized signatories as recorded in the demat account of the entity in whose favour such NDU is entered.

- On creation of freeze in the depository system, the depository/ participant of the BO holding shares, shall inform both parties of the NDU regarding creation of freeze under NDU.
- The depositories shall make suitable provisions for capturing the details of company/ promoters if they are part of the NDU.
- In case if the participant does not create the NDU, it shall intimate the same to the parties of the NDU along with the reasons thereof.
- Once the freeze for debits is created under the NDU for a particular quantity of shares, the depository shall not facilitate or effect any transfer, pledge, hypothecation, lending, rematerialisation or in any manner alienate or otherwise allow dealing in the shares held under NDU till receipt of instructions from both parties for the cancellation of NDU.
- The entry of NDU made above may be cancelled by the depository/ participant of the BO through unfreeze of specified quantity if parties to the NDU jointly make such application to the depository through the participant of the BO.
- On unfreeze of shares upon termination/ cancellation of NDU, the depository shall inform both parties of the NDU in the form and manner agreed upon at the time of creating the freeze. The unfreeze shall be effected in the depository system after a cooling period of 2 clear business days but no later than 4 clear business days.

The freeze and unfreeze instructions executed by the Participant for recording NDUs will be subject to 100% concurrent audit. The DPs shall not facilitate or be a party to any NDU outside the depository system as outlined herein.

PLEDGE OR HYPOTHECATION OF SECURITIES HELD IN A DEPOSITORY

A beneficial owner may with the previous approval of the depository create a pledge or hypothecation in respect of a security owned by him through a depository. Every beneficial owner should give intimation of such pledge or hypothecation to the depository participant and such depository is required to make entries in its records accordingly. Any entry in the records of a depository should be evidence of a pledge or hypothecation.

FURNISHING OF INFORMATION AND RECORDS BY DEPOSITORY AND ISSUER

Every depository shall furnish to the issuer information about the transfer of securities in the name of beneficial owners at such intervals and in such manner as may be specified by the bye-laws. Every issuer shall make available to the depository copies of the relevant records in respect of securities held by such depository.

OPTION TO OPT OUT IN RESPECT OF ANY SECURITY

Section 14 of the Act provides that if a beneficial owner seeks to opt out of a depository in respect of any security he should inform the depository accordingly. After the receipt of intimation the depository should make appropriate entries in its records and also inform the issuer. Every issuer may, within thirty days of the receipt of intimation from the depository and on fulfillment of such conditions and on payment of such fees as may be specified by the regulations, issue the certificate of securities to the beneficial owner or the transferee, as the case may be.

DEPOSITORIES TO INDEMNIFY LOSS IN CERTAIN CASES

Any loss caused to the beneficial owner due to the negligence of the depository or the participant, would be

indemnified by the depository to such beneficial owner. Where the loss due to the negligence of the participant is indemnified by the depository, the depository has the right to recover the same from such participant.

FRAMEWORK OF CAPACITY PLANNING FOR THE DEPOSITORIES

SEBI has issued Capacity Planning Framework for the Depositories which prescribes mandatory requirements for depositories while planning capacities for their operations as discussed below:

- The installed capacity shall be at least 1.5 times of the projected peak load.
- The projected peak load shall be calculated for the next 60 days based on the per hour peak load trend of the past 180 days.
- The Depositories shall ensure that the utilisation of resources in such a manner so as to achieve work completion in 70% of the allocated time.
- All systems pertaining to Depository operations shall be considered in this process including all technical components such as network, hardware, software, etc., and shall be adequately sized to meet the capacity requirements.
- In case the actual capacity utilisation exceeds 75% of the installed capacity for a period of 15 days on a rolling basis, immediate action shall be taken to enhance the capacity.
- The actual capacity utilisation shall be monitored especially during the period of the day in which pay-in and pay-out of securities takes place for meeting settlement obligations.

Depositories shall implement suitable mechanisms, including generation of appropriate alerts, to monitor capacity utilisation on a real-time basis and shall proactively address issues pertaining to their capacity needs.

POWER OF SEBI

Section 18 of the Act provides that SEBI in the public interest or in the interest of investors may by order in writing to call upon any issuer, depository, participant or beneficial owner to furnish in writing such information relating to the securities held in a depository as it may require; or authorise any person to make an enquiry or inspection in relation to the affairs of the issuer, beneficial owner, depository or participant, who shall submit a report of such enquiry or inspection to it within such period as may be specified in the order.

Sub-section (2) to Section 18 provides that every director, manager, partner, secretary, officer or employee of the depository or issuer or the participant or beneficial owner shall on demand produce before the person making the enquiry or inspection all information or such records and other documents in his custody having a bearing on the subject matter of such enquiry or inspection.

POWER OF SEBI TO GIVE DIRECTIONS

Section 19 provides that SEBI after making or causing to be made an enquiry or inspection SEBI is satisfied that it is necessary in the interest of investors or the securities market or to prevent the affairs of any depository or participant being conducted in the manner detrimental to the interests of investors or the securities market.

it may issue such directions, –

- (a) to any depository or participant or any person associated with the securities market; or
- (b) to any issuer, as may be appropriate in the interest of investors or the securities market

POWER TO ADJUDICATE

Section 19H provides that for the purpose of adjudging SEBI shall appoint any officer not below the rank of a Division Chief of SEBI to be an adjudicating officer for holding an inquiry in the prescribed manner after giving

any person concerned a reasonable opportunity of being heard for the purpose of imposing any penalty. While holding an inquiry, the adjudicating officer shall have power to summon and enforce the attendance of any person acquainted with the facts and circumstances of the case to give evidence or to produce any document, which in the opinion of the adjudicating officer, may be useful for or relevant to the subject matter of the inquiry and if, on such inquiry, he is satisfied that the person has failed to comply with the provisions of any of the sections specified in this Act, he may impose such penalty as he thinks fit in accordance with the provisions of any of those sections.

Section 19H(3) empowered SEBI to call for and examine the record of any proceedings under this section and if it considers that the order passed by the adjudicating officer is erroneous to the extent it is not in the interest of the securities market, it may, after making or causing to be made such inquiry as it deems necessary, pass an order enhancing the quantum of penalty, if the circumstances of the case so justify.

However, no such order shall be passed unless the person concerned has been given an opportunity of being heard in the matter. Further, nothing contained in this sub-section shall be applicable after an expiry of a period of three months from the date of the order passed by the adjudicating officer or disposal of the appeal under section 23A, whichever is earlier.

POWER TO GRANT IMMUNITY

Section 22B empowers the Central Government to grant immunity, on recommendation by the SEBI, if the Central Government is satisfied, that any person, who is alleged to have violated any of the provisions of this Act or the rules or the regulations made there under, has made a full and true disclosure in respect of alleged violation, grant to such person, subject to such conditions as it may think fit to impose, immunity from prosecution for any offence under this Act, or the rules or the regulations made there under or also from the imposition of any penalty under this Act with respect to the alleged violation. No such immunity shall be granted by the Central Government in cases where the proceedings for the prosecution for any such offence have been instituted before the date of receipt of application for grant of such immunity. Recommendation of SEBI under this sub-section is not binding upon the Central Government.

The immunity granted to a person may, at any time, be withdrawn by the Central Government, if it is satisfied that such person had, in the course of the proceedings, not complied with the condition on which the immunity was granted or had given false evidence, and thereupon such person may be tried for the offence with respect to which the immunity was granted or for any other offence of which he appears to have been guilty in connection with the contravention and shall also become liable to the imposition of any penalty under this Act to which such person would have been liable, had not such immunity been granted.

POWER OF SEBI TO MAKE REGULATIONS

Section 25 of the Depositories Act, 1996 read with Section 30 of SEBI Act, 1992 empowers SEBI to make regulations for carrying out the purposes of the Act, by notification in the Official Gazette. The regulations may, inter alia, provide for :

The form in which record is to be maintained under section 2(1)(i) –

- The form in which the certificate of commencement of business has to be issued.
- The manner in which the certificate of security shall be surrendered to the issuer by any investor who is desirous of availing depository services.
- The requirements to be complied with by a beneficial owner for creating with the previous approval of depository, pledge or hypothecation in respect of a security owned by him through depository.
- The conditions and the fees payable with respect to the issue of certificate of securities to the beneficial owner where the beneficial owner seeks to opt out of the depository.

- The rights and obligations of the depositories, participants, and the issuers whose securities are dealt with by a depository.
- The eligibility criteria for admission of securities into the depository.
- The terms determined by SEBI for settlement of proceeding under section 19-IA.
- Any other matter which is required to be, or may be, specified by regulations or in respect of which provisions to be made by regulations.

PENALTY FOR FAILURE TO FURNISH INFORMATION/RETURN ETC.

Section 19A provides that any person, who is required under Depositories Act or any rules or regulations or bye-laws made there under –

- (a) to furnish any information, document, books, returns or report to the Board, fails to furnish the same within the time specified therefor fails to furnish the same within specified time;
- (b) to file any return or furnish any information, books or other documents within the time specified therefor in the regulations or bye-laws, fails to file return or furnish the same within the time specified therefor, fails to file such return or furnish the required information within the specified time;
- (c) to maintain books of account or records, fails to maintain the same;

he shall be liable to a penalty of one lakh rupees for each day during which such failure continues or one crore rupees, whichever is less.

PENALTY FOR FAILURE TO ENTER INTO AGREEMENT

Section 19B provides that if a depository or participant or any issuer or its agent or any person, who is a registered intermediary and is required under this Act or any rules or regulations made there under, to enter into an agreement, fails to enter into such agreement, such intermediary shall be liable to a penalty of one lakh rupees for each day during which such failure continues or one crore rupees, whichever is less for every such failure.

PENALTY FOR FAILURE TO REDRESS INVESTORS' GRIEVANCES

Section 19C provides that if any depository or participant or any issuer or its agent or any person, who is registered as a registered intermediary, after having been called upon by the SEBI in writing, to redress the grievances of the investors, fails to redress such grievances within the time specified, such depository or participant or issuer or its agents or intermediary shall be liable to a penalty of one lakh rupees for each day during which such failure continues or one crore rupees, whichever is less.

PENALTY FOR DELAY IN DEMATERIALISATION OR ISSUE OF CERTIFICATE OF SECURITIES

Section 19D provides that if any issuer or its agent or any person, who is a registered intermediary, fails to dematerialise or issue the certificate of securities on opting out of a depository by the investors, within the time specified under this Act or regulations or bye-laws made there under or abets in delaying the process of dematerialisation or issue the certificate of securities on opting out of a depository of securities, such intermediary shall be liable to a penalty of one lakh rupees for each day during which such failure continues or one crore rupees, whichever is less.

PENALTY FOR FAILURE TO RECONCILE RECORDS

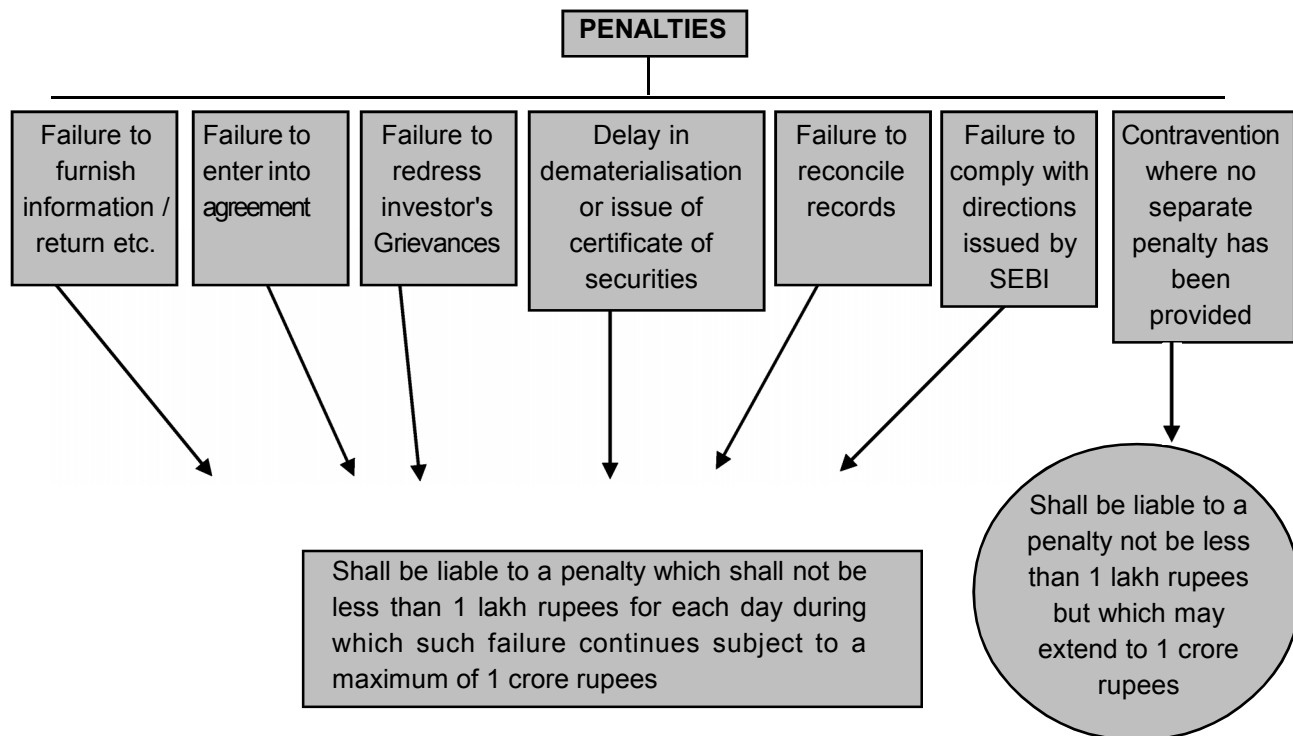
Section 19E provides that if a depository or participant or any issuer or its agent or any person, who is a registered intermediary, fails to reconcile the records of dematerialised securities with all the securities issued by the issuer as specified in the regulations, such intermediary shall be liable to a penalty of one lakh rupees for each day during which such failure continues or one crore rupees, whichever is less.

PENALTY FOR FAILURE TO COMPLY WITH DIRECTIONS ISSUED BY SEBI

Section 19F requires that if any person fails to comply with the directions issued by SEBI under section 19, within the time specified by it, he shall be liable to a penalty of one lakh rupees for each day during which such failure continues or one crore rupees, whichever is less.

PENALTY FOR CONTRAVENTION WHERE NO SEPARATE PENALTY HAS BEEN PROVIDED

Section 19G provides that whoever fails to comply with any provision of this Act, the rules or the regulations or bye-laws made or directions issued by SEBI thereunder for which no separate penalty has been provided, shall be liable to a penalty which may extend to one crore rupees.



FACTORS TO BE TAKEN INTO ACCOUNT BY ADJUDICATING OFFICER

Section 19 I requires that while adjudging the quantum of penalty under section 19H, the adjudicating officer shall have due regard to the following factors, namely—(a) the amount of disproportionate gain or unfair advantage, wherever quantifiable, made as a result of the default; (b) the amount of loss caused to an investor or group of investors as a result of the default; (c) the repetitive nature of the default.

Settlement of Administrative Civil Proceedings

Section 19-IA provides that any person, against whom any proceedings have been initiated or may be initiated under section 19, section 19H, as the case may be, may file an application in writing to SEBI proposing for settlement of the proceedings initiated or to be initiated for the alleged defaults.

Sub-section 2 authorises that SEBI may, after taking into consideration the nature, gravity and impact of defaults, agree to the proposal for settlement, on payment of such sum by the defaulter or on such other terms as may be determined by SEBI in accordance with the regulations made under the SEBI Act, 1992.

Sub-section 3 lays down that for the purpose of settlement under this section, the procedure specified by SEBI under the SEBI Act, 1992 shall apply. Further Sub-section 4 provides that no appeal shall lie under section 23A against any order passed by SEBI or the adjudicating officer, as the case may be, under this section.

Recovery of amounts

Section 19-IB deals with recovery of amounts by SEBI.

If a person fails to pay the penalty imposed by the adjudicating officer or fails to comply with a direction of disgorgement order issued under Section 19 or fails to pay any fees due to SEBI, the Recovery Officer may draw up under his signature a statement in the specified form specifying the amount due from the person (such statement being hereafter in this Chapter referred to as certificate) and shall proceed to recover from such person the amount specified in the certificate by one or more of the following modes, namely:-

- (a) attachment and sale of the person's movable property;
- (b) attachment of the person's bank accounts;
- (c) attachment and sale of the person's immovable property;
- (d) arrest of the person and his detention in prison;
- (e) appointing a receiver for the management of the person's movable and immovable properties,

and for this purpose, the provisions of section 220 to 227, 228A, 229, 232, the Second and Third Schedules to the Income-tax Act, 1961 and the Income-tax (Certificate Proceedings) Rules, 1962, as in force from time to time, in so far as may be, apply with necessary modifications as if the said provisions and the rules thereunder were the provisions of this Act and referred to the amount due under this Act instead of to income-tax under the Income-tax Act, 1961.

Explanation 1 – For the purpose of this sub-section, the person's movable or immovable property or monies held in bank accounts shall include any property or monies held in bank accounts which has been transferred directly or indirectly on or after the date when the amount specified in certificate had become due, by the person to his spouse or minor child or son's wife or son's minor child, otherwise than for adequate consideration, and which is held by, or stands in the name of, any of the persons aforesaid; and so far as the movable or immovable property or monies held in bank accounts so transferred to his minor child or his son's minor child is concerned, it shall, even after the date of attainment of majority by such minor child or son's minor child, as the case may be, continue to be included in the person's movable or immovable property or monies held in bank accounts for recovering any amount due from the person under this Act.

Explanation 2 – Any reference under the provisions of the Second and Third Schedules to the Income-tax Act, 1961 and the Income-tax (Certificate Proceedings) Rules, 1962 to the assessee shall be construed as a reference to the person specified in the certificate.

Explanation 3 – Any reference to appeal in Chapter XVIII and the Second Schedule to the Income-tax Act, 1961, shall be construed as a reference to appeal before the Securities Appellate Tribunal under Section 23A of this Act.

Sub-section (2) empowers the Recovery Officer to seek the assistance of the local district administration while exercising the powers under sub-section (1).

Sub-section (3) provides that the recovery of amounts by a Recovery Officer under sub-section (1), pursuant to non-compliance with any direction issued by SEBI under section 19, shall have precedence over any other claim against such person.

The expression "Recovery Officer" means any officer of SEBI who may be authorised, by general or special order in writing, to exercise the powers of a Recovery Officer.

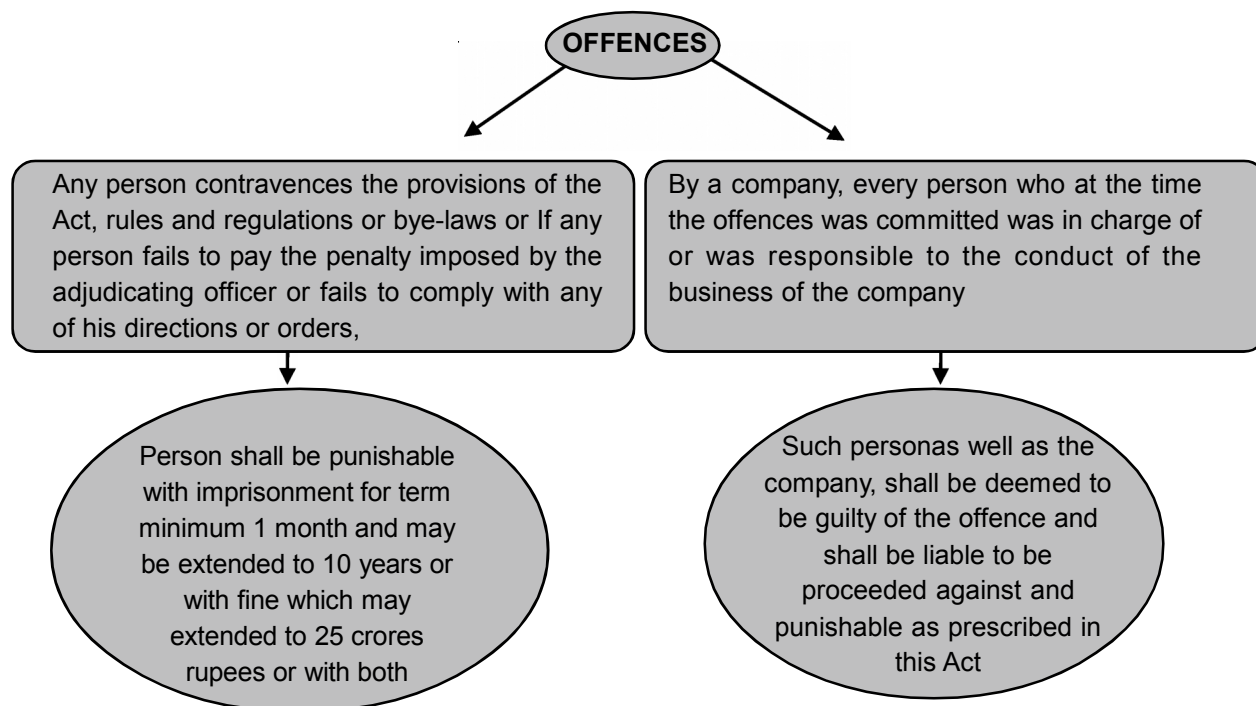
CREDITING OF PENALTIES TO CONSOLIDATED FUND OF INDIA

Section 19J provides that all sums realised by way of penalties under this Act shall be credited to the Consolidated Fund of India.

OFFENCES

Section 20 provides that without prejudice to any award of penalty by the adjudicating officer under this Act, if

any person contravenes or attempts to contravene or abets the contravention of the provisions of this Act or of any rules or regulations or bye-laws made there under, he shall be punishable with imprisonment for a term which may extend to ten years, or with fine, which may extend to twenty-five crore rupees, or with both. If any person fails to pay the penalty imposed by the adjudicating officer or fails to comply with any of his directions or orders, he shall be punishable with imprisonment for a term which shall not be less than one month but which may extend to ten years, or with fine, which may extend to twenty-five crore rupees, or with both.



OFFENCES BY COMPANIES

Section 21 provides that where an offence under this Act has been committed by a company, every person who at the time the offence was committed was in charge of, and was responsible to, the company for the conduct of the business of the company, as well as the company, shall be deemed to be guilty of the offence and shall be liable to be proceeded against and punished accordingly. The proviso to the section also provides that nothing contained in this sub-section shall render any such person liable to any punishment provided in this Act, if he proves that the offence was committed without his knowledge or that he had exercised all due diligence to prevent the commission of such offence. Where an offence under this Act has been committed by a company and it is proved that the offence has been committed with the consent or connivance of, or is attributable to any neglect on the part of, any director, manager, secretary or other officer of the company, such director, manager, secretary or other officer shall also be deemed to be guilty of the offence and shall be liable to be proceeded against and punished accordingly.

COGNIZANCE OF OFFENCES BY COURTS

Section 22 provides that no court shall take cognizance of any offence punishable under this Act or any rules or regulations or bye-laws made there under except on a complaint made by the Central Government or State Government or the SEBI or by any person.

COMPOSITION OF CERTAIN OFFENCES

Section 22A provides that notwithstanding anything contained in the Code of Criminal Procedure, 1973, any offence punishable under this Act, not being an offence punishable with imprisonment only, or with imprisonment

and also with fine, may either before or after the institution of any proceeding, be compounded by a Securities Appellate Tribunal or a court before which such proceedings are pending.

Establishment of Special Courts

Section 22C provides that the Central Government may, for the purpose of providing speedy trial of offences under this Act, by notification, establish or designate as many Special Courts as may be necessary. A Special Court shall consist of a single judge who shall be appointed by the Central Government with the concurrence of the Chief Justice of the High Court within whose jurisdiction the judge to be appointed is working. A person shall not be qualified for appointment as a judge of a Special Court unless he is, immediately before such appointment, holding the office of a Sessions Judge or an Additional Sessions Judge, as the case may be.

Offences triable by Special Courts

Section 22D provides that all offences under this Act committed shall be taken cognizance of and triable by the Special Court established for the area in which the offence is committed or where there are more Special Courts than one for such area, by such one of them as may be specified in this behalf by the High Court concerned.

Appeal and Revision

Section 22E authorises the High Court to exercise, so far as may be applicable, all the powers conferred by Chapters XXIX and XXX of the Code of Criminal Procedure, 1973 on a High Court, as if a Special Court within the local limits of the jurisdiction of the High Court were a Court of Session trying cases within the local limits of the jurisdiction of the High Court.

Application of Code to proceedings before Special Court

Section 22 lays down that the provisions of the Code of Criminal Procedure, 1973 shall apply to the proceedings before a Special Court and for the purposes of the said provisions, the Special Court shall be deemed to be a Court of Session and the person conducting prosecution before a Special Court shall be deemed to be a Public Prosecutor within the meaning of clause (u) of section 2 of the Code of Criminal Procedure, 1973. The person conducting prosecution under this section should have been in practice as an Advocate for not less than seven years or should have held a post, for a period of not less than seven years, under the Union or a State requiring special knowledge of law.

Transitional provisions

Section 22G stipulates that any offence committed under this Act, which is triable by a Special Court shall, until a Special Court is established, be taken cognizance of and tried by a Court of Session exercising jurisdiction over the area, notwithstanding anything contained in the Code of Criminal Procedure, 1973. However, nothing contained in this section shall affect the powers of the High Court, under section 407 of the Code to transfer any case or class of cases taken cognizance by a Court of Session under this Section.

Appeals

Section 23 deals with appeal to Central Government. Any person aggrieved by an order of SEBI under this Act, or the regulations made thereunder may prefer an appeal to the Central Government within such time as may be prescribed. No appeal shall be admitted if it is preferred after the expiry of the period prescribed therefor. However, an appeal may be admitted after the expiry of the period prescribed therefor if the appellant satisfies the Central Government that he had sufficient cause for not preferring the appeal within the prescribed period. Every appeal made under this section shall be made in such form and shall be accompanied by a copy of the order appealed against and by such fees as may be prescribed. The procedure for disposing of an appeal shall be such as may be prescribed. However, before disposing of an appeal, the appellant shall be given a reasonable opportunity of being heard.

APPEAL TO SECURITIES APPELLATE TRIBUNAL

Section 23A provides that, any person aggrieved by an order of SEBI under this Act, or the regulations made thereunder or an order made by an adjudicating officer under this Act, may prefer an appeal to a Securities Appellate Tribunal having jurisdiction in the matter. Every appeal shall be filed within a period of forty-five days from the date on which a copy of the order made by SEBI is received by the person and it shall be in such form and be accompanied by such fee as may be prescribed.

However, the Securities Appellate Tribunal may entertain an appeal after the expiry of the said period of forty-five days if it is satisfied that there was sufficient cause for not filing it within that period.

On receipt of an appeal, the Securities Appellate Tribunal may, after giving the parties to the appeal an opportunity of being heard, pass such orders thereon as it thinks fit, confirming, modifying or setting aside the order appealed against.

The Securities Appellate Tribunal shall send a copy of every order made by it to SEBI and parties to the appeal. The appeal filed before the Securities Appellate Tribunal shall be dealt with by it as expeditiously as possible and endeavour shall be made by it to dispose of the appeal finally within six months from the date of receipt of the appeal.

PROCEDURE AND POWERS OF SECURITIES APPELLATE TRIBUNAL

Section 23B provides that the Securities Appellate Tribunal shall not be bound by the procedure laid down by the Code of Civil Procedure, 1908, but shall be guided by the principles of natural justice and, subject to the other provisions of this Act and of any rules, the Securities Appellate Tribunal shall have powers to regulate their own procedure including the places at which they shall have their sittings. The Securities Appellate Tribunal shall have, for the purpose of discharging their functions under this Act, the same powers as are vested in a civil court under the Code of Civil Procedure, 1908, while trying a suit, in respect of the following matters, namely—

- (a) summoning and enforcing the attendance of any person and examining him on oath;
- (b) requiring the discovery and production of documents;
- (c) receiving evidence on affidavits;
- (d) issuing commissions for the examination of witnesses or documents;
- (e) reviewing its decisions;
- (f) dismissing an application for default or deciding it ex parte;
- (g) setting aside any order of dismissal of any application for default or any order passed by it ex parte; and
- (h) any other matter which may be prescribed.

Every proceeding before the Securities Appellate Tribunal shall be deemed to be a judicial proceeding within the meaning of sections 193 and 228, and for the purposes of section 196 of the Indian Penal Code and the Securities Appellate Tribunal shall be deemed to be a civil court for all the purposes of section 195 and Chapter XXVI of the Code of Criminal Procedure, 1973.

RIGHT TO LEGAL REPRESENTATION

Section 23C provides that the appellant may either appear in person or authorise one or more Chartered Accountants or Company Secretaries or Cost Accountants, in practice or Legal Practitioners or any of its officers to present his/its case before the Securities Appellate Tribunal.

LIMITATIONS

Section 23 D provides that the provisions of the Limitation Act, 1963 shall, as far as may be, apply to an appeal made to a Securities Appellate Tribunal.

CIVIL COURT NOT TO HAVE JURISDICTION

Section 23 E provides that no Civil Court shall have jurisdiction to entertain any suit or proceeding in respect of any matter which a Securities Appellate Tribunal is empowered by or under this Act to determine and no injunction can be granted by any court or other authority in respect of any action taken or to be taken in pursuance of any power conferred by or under this Act.

APPEAL TO SUPREME COURT

Section 23F provides that any person aggrieved by any decision or order of the Securities Appellate Tribunal may file an appeal to the Supreme Court within sixty days from the date of communication of the decision or order of the Securities Appellate Tribunal to him on any question of law arising out of such order. However, that the Supreme Court may, if it is satisfied that the appellant was prevented by sufficient cause from filing the appeal within the said period, allow it to be filed within a further period not exceeding sixty days.

AREAS ON WHICH RULES MAY BE FRAMED BY THE CENTRAL GOVERNMENT

The Central Government under Section 24, may frame Rules to provide, inter alia, for:

- the manner of inquiry under Section 19H(1).
- the time within which an appeal may be preferred from the orders of SEBI under Section 23(1).
- the form in which an appeal may be preferred and the fees payable in respect of such appeal.
- the procedure for disposing of an appeal.
- the form in which an appeal may be filed before the Securities Appellate Tribunal under Section 23A and the fees payable in respect of such appeal.

BYE-LAWS OF A DEPOSITORY

Section 26 deals with the power of depository to make bye-law. Depository is required to frame its bye-laws with the prior approval of SEBI, consistent with the provisions of the Act and the regulations made by SEBI thereunder. SEBI has, however, the power to direct the depository to amend or revoke any bye-laws already made, wherever it considers expedient to do so. If the depository fails or neglects to comply with the directions of SEBI, SEBI may make the bye-laws or amend or revoke the bye-laws on its own.

CONTENTS OF THE BYE-LAWS

As per Sub-section 2 of Section 26 of the Act, the bye-laws of a depository would include:

- the eligibility criteria for admission and removal of securities in the depository.
- the conditions subject to which the securities shall be dealt with.
- the eligibility criteria for admission of any person as a participant.
- the manner and procedure for dematerialisation of securities.
- the procedure for transactions within the depository.
- the manner in which securities are to be dealt with or withdrawn from a depository.
- the procedure for ensuring safeguards to protect the interests of participants and beneficial owners.
- the conditions of admission into and withdrawal from a participant by a beneficial owner.
- the procedure for conveying information to the participants and beneficial owners on dividend declaration, shareholder meetings and other matters of interest to the beneficial owners.

- the manner of distribution of dividends, interest and monetary benefits received from the company among beneficial owners.
- the manner of creating pledge or hypothecation in respect of securities held with a depository.
- *inter-se* rights and obligations among the depository, issuer, participants and beneficial owners.
- the manner and the periodicity of furnishing information to SEBI, issuer and other persons.
- the procedure for resolving disputes involving depository, issuer company or a beneficial owner.
- the procedure for proceeding against the participant committing breach of the regulations and provisions for suspension and expulsion of participants from the depository and cancellation of agreements entered with the depository.
- the internal control standards including procedure for auditing, reviewing and monitoring.

MEMBERSHIP RIGHTS IN RESPECT OF SECURITIES HELD BY A DEPOSITORY

The depository as a registered owner shall not have any voting rights or any other rights in respect of securities held by it on behalf of the beneficial owners. The beneficial owner shall be entitled to all the rights and benefits (including the right to vote) and be subjected to all the liabilities in respect of securities held by a depository.

EVIDENCIARY VALUE OF THE RECORDS OF THE DEPOSITORY

Section 15 of the Act treats depository as a bank for the purposes of the Bankers' Books Evidence Act, 1891. The ownership records of securities maintained by depositories, whether maintained in the form of books or machine readable forms, shall be accepted as *prima facie* evidence in all legal proceedings.

SEBI (DEPOSITORIES AND PARTICIPANTS) REGULATIONS, 1996

The Depositories Act requires that the registration of the depository, depository participant and the custodian, is mandatory with the SEBI. These market intermediaries can function or commence business only after registration from SEBI has been obtained and requisite fee paid to SEBI. The requirement of registration is a continuing one and the moment of registration is cancelled or revoked or surrendered, the person shall cease to act as such.

SEBI had issued SEBI (Depositories and Participants) Regulations, 1996 on 16th May, 1996 which apply to depositories and its participants.

These regulations also contain provisions for operations and functioning of depositories, form for application and certificates used and schedule of fees for participants, etc. It also contains provisions for registration of depository and depository participants, rights and obligations of various users and constituents, inspection and procedure for action in case of default.

Entities desiring to become depository participants must apply to the depository and are required to be recommended to SEBI by the depository. If approved and registered by SEBI, the depository participant can be admitted on the depository. The depository has to formulate its own set of criteria for selection of participants. Every participant holding a certificate is required at all times to abide by the specified Code of Conduct.

The regulations require the depository to list out, through its bye-laws, the securities which are eligible to be admitted to the depository for dematerialization. Equity shares, debentures, warrants, bonds, units of mutual funds, etc. are part of the list of eligible securities. The depository is empowered to set its own criteria for selection of securities and make securities eligible to be maintained in the form of electronic holdings on the depository.

Further, the regulations stipulate that agreements should be entered into by the following entities:

- depository and every participant;
- participant and every client; and
- depository, issuer company and the Registrar.

The draft of these agreements are to be included in the bye-laws and to be approved by SEBI.

The depository is required to ensure that sufficient safeguards are in place to protect the data available with it and with the participants. To reduce risk in operations, the regulations stipulate that adequate insurance cover be provided by the depository and by the depository participants as well.

The regulations also require for reconciliation to be carried out on a daily basis. Further, the depository and the registrar will also reconcile balances on a daily and a periodic basis.

RIGHTS AND OBLIGATIONS OF DEPOSITORIES AND ITS CONSTITUENTS

This Regulations deal with rights and obligations of depositories and every depository has to state in its bye-laws the eligible securities for dematerialisation which include shares, scrips, stock, bonds, debentures stock, Indian Depository Receipts or other marketable securities of a like nature, etc., and include units of mutual funds, rights under collective investment schemes and venture capital funds, commercial paper, certificate of deposit, securitised debt, money market instruments, Government Securities and even unlisted securities.

Every depository is required to enter into an agreement with the issuer in respect of securities disclosed as eligible to be held in demat form. No agreement is required to be entered into where the depository itself is an issuer of securities.

However, no such agreement shall be required to be entered into where the State or the Central Government is the issuer of Government Securities.

The depository is also required to enter into a tripartite agreement with the issuer, its transfer agent and itself where company has appointed a transfer agent. Every depository is required to maintain continuous connectivity with issuers, registrars and transfer agents, participants and clearing house or clearing corporations. Depositories should take adequate measures including insurance to protect the interest of the beneficial owners.

Every depository is required to maintain the following records and documents namely:

- records of securities dematerialised and rematerialised;
- the names of the transferor, transferee, and the dates of transfer of securities;
- a register and an index of beneficial owners;
- details of holding of the securities of the beneficial owners as at the end of the each day;
- records of instruction(s) received from and sent to participants, issuers, issuers' agents and beneficial owners;
- records of approval, notice, entry and cancellation of pledge or hypothecation, as the case may be;
- details of participants;
- details of securities declared to be eligible for dematerialisation in the depository; and
- such other records as may be specified by SEBI for carrying on the activities as a depository.

Every depository has to intimate SEBI the place where the records and documents are maintained.

Subject to the provisions of any other law, the depository shall preserve records and documents for a minimum period of five years.

Participants are required to enter into an agreement with beneficial owners. It is required that separate accounts are to be opened by every participant in the name of each of the beneficial owner and the securities of each beneficial owners are to be segregated and shall not be mixed up with the securities of other beneficial owners or with the participant's own securities. The participants are obliged to reconcile the records with every depository on a daily basis. Participants are required to maintain the following records for a period of five years–

- records of all the transactions entered into with a depository and with a beneficial owner;
- details of security dematerialised, rematerialised on behalf of beneficial owners with whom it has entered into an agreement;
- records of instructions received from beneficial owners;
- statements of account provided to beneficial owners; and
- records of approval, notice, entry and cancellation of pledge or hypothecation as the case may be.

GOVERNANCE OF DEPOSITORY

Governing Board, Disclosures and Corporate Governance

This regulations deal with the composition of Governing board of a Depository.

- The governing board of every depository is required to include:
 - (a) shareholder directors;
 - (b) public interest directors; and
 - (c) managing director.
- Any employee of a depository may be appointed on the governing board in addition to the managing director, and such director shall be deemed to be a shareholder director.
- The chairperson shall be elected by the governing board from amongst the public interest directors Subject to prior approval of SEBI.
- The number of public interest directors shall not be less than the number of shareholder directors in a depository.
- The managing director shall be an ex-officio director on the governing board and shall not be included in either the category of public interest directors or shareholder directors.

The disclosure requirements and corporate governance norms as specified for listed companies shall mutatis mutandis apply to a depository.

Investor Protection Fund of Depositories

Regulation 53C provides that every depository shall establish and maintain an Investor Protection Fund (IPF) for the protection of interest of beneficial owners. However, this fund shall not be used by the depository for the purpose of indemnifying the beneficial owner under section 16 of the Depositories Act, 1996.

Every depository shall credit five per cent or such percentage as may be specified by SEBI, of its profits from depository operations every year to the Investor Protection Fund.

Utilization of the IPF

The IPF may be utilized for the following purposes with a focus on depository related services:

- Promotion of investor education and investor awareness programmes through seminars, lectures, workshops, publications (print and electronic media), training programmes etc. aimed at enhancing securities market literacy and promoting retail participation in securities market.

- To aid, assist, subsidise, support, promote and foster research activities for promotion/ development of the securities market.
- To utilize the fund for supporting initiatives of Depository Participants for promotion of investor education and investor awareness programmes.
- To utilize the fund in any other manner as may be prescribed/ permitted by SEBI in the interest of investors.

Depositories shall frame their internal guidelines on utilisation of the funds in accordance with the aforementioned objectives and post approval of their board of directors, submit the same within 30 days to SEBI. Depositories shall also keep SEBI informed of any subsequent changes in internal guidelines with regard to utilization of IPF.

Constitution and Management of the IPF

The IPF shall be administered by way of a Trust created for the purpose:

- The IPF Trust shall consist of atleast:
 - a) one Public Interest Director (PID) of the depository,
 - b) one person of eminence from an academic institution from the field of finance / an expert in the field of investor education / a representative from the registered investor associations, recognized by SEBI and managing director of the depository.
- The depository shall provide the secretariat for the IPF Trust.
- The depository shall ensure that the funds in the IPF are kept in a separate account designated for this purpose and that the IPF is immune from any liabilities of the depository.

Contribution to the IPF

The following contributions shall be made by the depository to the IPF:

- 5% of their profits from depository operations every year.
- All fines and penalties recovered from DPs and other users including clearing member pool account penalty as specified in SEBI circular no. SMDRP/Policy/Cir-05/2001 dated February 01, 2001.
- Interest or Income received out of any investments made from the IPF.
- Funds lying to the credit of IPR (Investor Protection Reserve) / BOPF (Beneficial Owners Protection Fund) of the depository or any other such fund / reserve of the depository shall be transferred to IPF.
- Any other sums as may be prescribed by SEBI from time to time.

Investments of Fund

- Funds of the trust shall be invested in instruments such as Central Government securities, fixed deposits of scheduled banks and any such instruments which are allowed as per the investment policy approved by the board of the depository.
- The investment policy shall be devised with an objective of capital protection along with highest degree of safety and least market risk.
- The balance available in the IPF as at the end of the month and the amount utilised during the month including the manner of utilization, shall be reported in the monthly development report of the depository.

Business Continuity Plan

A depository shall have adequate Business Continuity Plan for data and electronic records to prevent, prepare for and recover from any disaster.

Wind-down Plan

Regulation 35B of the SEBI (Depositories and Participants) Regulations, 1996, every depository shall devise

and maintain a wind-down plan in accordance with guidelines specified by SEBI.

Meaning of Wind-Down Plan

A process or plan of action employed, for transfer of the beneficial owner accounts and other operational powers of the depository to an alternative institution that would take over the operations of the depository in scenarios such as erosion of networth of the depository or its insolvency or its inability to provide critical depository operations or services.

Audit Under SEBI (Depositories and Participants) Regulations, 1996

Regulation 55A of SEBI (Depositories and Participants) Regulations, 1996 provides that every issuer shall submit audit report on a quarterly basis to the concerned stock exchanges audited by a practicing Company Secretary or a qualified Chartered Accountant, for the purposes of reconciliation of the total issued capital, listed capital and capital held by depositories in dematerialized form, the details of changes in share capital during the quarter and the in-principle approval obtained by the issuer from all the stock exchanges where it is listed in respect of such further issued capital.

The audit report is required to give the updated status of the register of members of the issuer and confirm that securities have been dematerialized as per requests within 21 days from the date of receipt of requests by the issuer and where the dematerialization has not been effected within the said stipulated period, the report would disclose the reasons for such delay.

The issuer is under an obligation to immediately bring to the notice of the depositories and the stock exchanges, any difference observed in its issued, listed, and the capital held by depositories in dematerialized form.

INTERNAL AUDIT OF OPERATIONS OF DEPOSITORY PARTICIPANTS

The two Depository service providers in India, viz., National Securities Depository Ltd. (NSDL) and Central Depository Services (India) Limited (CDS) have allowed Company Secretaries in Whole-time Practice to undertake internal audit of the operations of Depository Participants (DPs).

NSDL has vide its circular No. NSDL/SG/II/010/99 dated 26th March 1999 notified amendment of its Bye Law 10.3.1 of Chapter 10 as follows:

10.3.1 "Every Participant shall ensure that an internal audit in respect of the operations of the Depository is conducted at intervals of not more than three months by a qualified Chartered Accountant or a Company Secretary holding a certificate of Practice and a copy of the internal audit report shall be furnished to the Depository."

CDSL has vide its letter dated September 28, 1999 notified amendment of its Bye Laws 16.3.1 as follows:

16.3.1 "Every Participant shall ensure that an internal audit shall be conducted in respect of the participant's operations relating to CDS by a qualified Chartered Accountant in accordance with the provisions of the Chartered Accountants Act, 1949 or by a Company Secretary in practice in accordance with the provisions of the Company Secretaries Act, 1980, at such intervals as may be specified by CDS from time to time. A copy of Internal Audit report shall be furnished to CDS."

CONCURRENT AUDIT

National Securities Depository Limited vide its Circular No. NSDL/POLICY/ 2006/0021 dated June 24, 2006 provides for concurrent audit of the Depository Participants. The Circular provides that w.e.f. August 1, 2006, the process of demat account opening, control and verification of Delivery Instruction Slips (DIS) is subject to Concurrent Audit. Depository Participants have been advised to appoint a firm of qualified Chartered Accountant(s) or Company Secretary(ies) holding a certificate of practice for conducting the concurrent audit. However, the participants in case they so desire, may entrust the concurrent audit to their Internal Auditors.

In respect of account opening, the auditor should verify all the documents including KYC documents furnished

by the Clients and verified by the officials of the Participants. The scope of concurrent audit with respect to control and verification of DIS cover the areas given below:

(I) Issuance of DIS

The procedure followed by the Participants with respect to:

- (a) Issuance of DIS booklets including loose slips.
- (b) Existence of controls on DIS issued to Clients including pre-stamping of Client ID and unique pre-printed serial numbers.
- (c) Record maintenance for issuance of DIS booklets (including loose slips) in the back office.

(II) Verification of DIS

The procedure followed by the Participants with respect to:

- (a) Date and time stamping (including late stamping) on instruction slips.
- (b) Blocking of used/reported lost/stolen instruction slips in back office system/ manual record.
- (c) Blocking of slips in the back office system/manual record which are executed in DPM directly.
- (d) Two step verification for a transaction for more than Rs. 5 lakh, especially in case of off-market transactions.
- (e) Instructions received from dormant accounts.

The Concurrent Auditor should conduct the audit in respect of all accounts opened, DIS issued and controls on DIS as mentioned above, during the day, by the next working day. In case the audit could not be completed within the next working day due to large volume, the auditor should ensure that the audit is completed within a week's time.

Any deviation and/or non-compliance observed in the aforesaid areas should be mentioned in the audit report of the Concurrent Auditor. The Management of the Participant should comment on the observations made by the Concurrent Auditor. The Concurrent Audit Report should be submitted to NSDL, on a quarterly basis, in a hard copy form. If the Auditor for Internal and Concurrent Audit is the same, consolidated report may be submitted.

ESTABLISHMENT OF CONNECTIVITY WITH NSDL AND CDSL

To enhance the efficiency of the stock market, rolling settlement were introduced by SEBI. To facilitate the settlement, SEBI prescribed the compulsory dematerialized trading by companies through connectivity with both the depositories NSDL and CDSL.

The stock exchanges may consider shifting the trading of securities of the Companies who have established connectivity with both the depositories to normal rolling settlement subject to the following:

- (a) At least 50% of non-promoter holdings are in demat mode before shifting the trading in the securities of the company from Trade for Trade Settlement (TFTS) to Normal Rolling Settlement.

For this purpose, the listed companies are required to obtain a certificate from its Registrar and Transfer Agent (RTA) and submit the same to the stock exchange/s. However, if an issuer company does not have a separate RTA, it may obtain a certificate in this regard from a practicing Company Secretary/ Chartered Accountant and submit the same to the stock exchange/s.

- (b) There are no other grounds/reasons for continuation of the trading in TFTS.

The Stock Exchanges are also required to report to SEBI, the action taken in this regard in their Monthly/ Quarterly Development Report.

APPOINTMENT OF COMMON AGENCY FOR SHARE REGISTRY WORK

In many cases the issuer companies are having an internal department or a division (by whatever name called)

for handling of physical share work and an outside agency for handling the work of electronic connectivity. This kind of arrangement is leading to delay in dematerialization, non-reconciliation of shareholding due to lack of proper co-ordination among the concerned agencies or departments, which is adversely affecting the interest of the investors.

SEBI therefore vide its circular D&CC/FITTC/CIR-15/2002 dated December 27, 2002 decided that all the work related to share registry in terms of both physical and electronic should be maintained at a single point i.e. either in-house by the company or by a SEBI registered R & T Agent.

Further SEBI vide its circular D&CC/FITTC/CIR – 17/2002 dated December 31, 2002 directed all the registrars and share transfer agents (RSTA) that:

1. They shall maintain records of all the shares dematerialized, rematerialized and details of all securities declared to be eligible for dematerialization in the depositories and ensure that dematerialization of shares shall be confirmed/created only after an in-principle approval of the stock exchange/s where the shares are listed and the admission of the said share with the depositories have been granted.
2. They shall have proper systems and procedures in place to verify that the securities tendered for dematerialization have not been dematerialized earlier.
3. They shall ascertain, reconcile daily and confirm to the depositories that the total number of shares held in NSDL, CDSL and in the physical form tallies with the admitted, issued and listed capital of the issuer company; and
4. They shall confirm that the dematerialization requests have been processed within 21 days and shall also state the reasons for shares pending confirmation for more than 21 days from the date of request.

IN-PERSON VERIFICATION (IPV)

- SEBI has made it mandatory for all the intermediaries including Depository Participant (DP) to carry out IPV of their clients.
- The intermediary shall ensure that the details like name of the person doing IPV, his designation, organization with his signatures and date are recorded on the KYC form at the time of IPV.
- The IPV carried out by one SEBI registered intermediary can be relied upon by another intermediary.

DESIGNATED DEPOSITORY PARTICIPANT (DDP)

“Designated depository participant” means a person who has been approved by SEBI under Chapter III of SEBI (Foreign Portfolio Investors) Regulations, 2014. A person shall not act as designated depository participant unless it has obtained the approval of SEBI.

Eligibility criteria for DDP

SEBI shall grant an approval to a person to act as DDP subject to satisfaction of, *inter alia*, the following conditions:

- (a) The applicant is a participant and custodian registered with the SEBI;
- (b) The applicant is an Authorized Dealer Category-1 bank authorized by the Reserve Bank of India;
- (c) The applicant has multinational presence either through its branches or through agency relationships with intermediaries regulated in their respective home jurisdictions;
- (d) The applicant has systems and procedures to comply with the requirements of FATF Standards, Prevention of Money Laundering Act, 2002, and the rules and circulars prescribed thereunder.
- (e) A Certificate of Registration granted to a DDP shall be permanent unless suspended or cancelled by SEBI or surrendered by the DDP.

On 7 January 2014, SEBI notified the SEBI (Foreign Portfolio Investors) Regulations, 2014 (FPI Regulations). Subsequently, the SEBI has also vide a Circular dated 8 January 2013 issued operating guidelines for Designated Depository Participants (DDP) who would grant registration to Foreign Portfolio Investors (FPI). Designated Depository Participants (DDPs) are authorised to grant registration to FPIs on behalf of the SEBI. The application for grant of registration is to be made to the DDP in a prescribed form alongwith the specified fees.

BASIC SERVICES DEMAT ACCOUNT (BSDA)

With a view to achieve wider financial inclusion, encourage holding of demat accounts and to reduce the cost of maintaining securities in demat accounts for retail individual investors, SEBI introduced the concept of basic services demat account (BSDA). All depository participants (DPs) shall make available a "Basic Services Demat Account" (BSDA) with limited services and reduced costs compared to conventional demat accounts. These BSDA will also offer SMS alert facility for debit transactions.

Eligible Investor

The "Basic Services Demat Account" (BSDA) promises to provide limited services at reduced costs to retail investors. All individual who currently have one account or plan to open an demat account where they are the sole or first holder will be allowed to open the BSDA. However, the value of securities held will not be more than ₹ 2 lakh at any given point of time. However, Investors can open only one BSDA across all DPs.

An existing eligible individual who holds a demat account with a DP can convert demat account into BSDA on the date of the next billing cycle based on value of holding of securities as on the last day of previous billing cycle.

SEBI vide its circular dated December 11, 2015 advised the DPs to convert all the eligible demat accounts into BSDA unless such Beneficial Owners (BOs) specifically OPT continue to avail the facilities of a regular demat account.

Charges

The Annual Maintenance Charges (AMC) which will have to pay for BSDA will be as per pre-determined slabs. If the value of holdings is up to ₹ 50,000 there won't be any annual maintenance charge. However, if the value of holding is in between ₹ 50,001 to ₹ 200,000, a fee of ₹ 100 as AMC may be charged. If the value of holdings exceeds, DPs are permitted to charge the same as they charge non- BSDA regular demat accounts.

Valuation of Holding

The value of holding shall be determined on the basis of the daily closing price or Net Asset Value of the securities or units of mutual funds. Where such price is not available the last traded price may be taken into account and for unlisted securities other than units of mutual funds, face value may be taken into account.

Statements

(a) Transaction statements:

- (a) Transaction statements shall be sent to the beneficial owner (BO) at the end of each quarter. If there are no transactions in any quarter, no transaction statement may be sent for that quarter.
- (b) If there are no transactions and no security balance in an account, then no further transaction statement needs to be provided.
- (c) Transaction statement shall be required to be provided for the quarter in which the account became a zero balance account.

(b) Holding Statement:

- (a) One annual physical statement of holding shall be sent to the stated address of the BO in respect of accounts with no transaction and nil balance.

- b) One annual statement of holding shall be sent in respect of remaining accounts in physical or electronic form as opted for by the BO.

Charges for statements

Electronic statements shall be provided free of cost. However, for physical statements, DPs have to provide two statements free of cost to the account holder during the billing cycle. But additional statements will be charged a fee, which cannot be more than ₹ 25. All BOs opting for the facility of BSDA shall register their mobile number for availing the SMS alert facility for debit transaction. At least two delivery instruction slip shall be issued at the time of account opening.

However, in order to reduce the cost of compliance of DPs, the following rationalization measures have been prescribed for regular accounts:

- (a) Accounts with zero balance and nil transactions during the year: The DPs shall send one physical statement of holding annually to such BOs and shall resume sending the transaction statement as and when there is a transaction in the account.
- (b) Accounts which become zero balance during the year: For such accounts, no transaction statement may be sent for the duration when the balance remains nil. However, an annual statement of holding shall be sent to the Beneficiary Owner.
- (c) Accounts with credit balance: For accounts with credit balance but no transactions during the year, one statement of holding for the year shall be sent to the BO.

SINGLE REGISTRATION FOR DEPOSITORY PARTICIPANTS

SEBI vide its circular dated December 24, 2014 amended the SEBI (Depositories and Participants) Regulations by inserting a new regulation 20AB regarding 'acting as participant in more than one depository.' Further, as per this amendment the existing requirement of obtaining certificate of initial registration to act as a participant and subsequently permanent registration to continue to act as a participant for each depository has been done away with by SEBI. Henceforth, one certificate of initial registration and subsequently permanent registration through any depository shall be required.

For the purpose of single registration, the following guidelines are being issued:

- If a new entity desires to act as a participant in any of the depository, then the entity shall apply to SEBI for certificate of initial registration through the concerned depository in the manner prescribed in the DP Regulations.
- If an entity has been granted a certificate of registration to act as a participant through one depository and wishes to act as a participant with the other depository then it shall directly apply to the concerned depository for approval in the manner as prescribed in the DP Regulations.
- The concerned depository, on receipt of the application, may grant approval to the entity after exercising due diligence and on being satisfied about the compliance of all relevant eligibility requirements including the following:
 - (a) The applicant, its directors, proprietor, partners and associates shall be fit and proper.
 - (b) The applicant has taken satisfactory corrective steps to rectify the deficiencies or irregularities observed in the past inspections or in case of actions initiated/ taken by SEBI/ depository(s) or other regulators.
 - (c) Recovery of all pending fees/ dues payable to SEBI and depository; and
 - (d) Payment of registration fees as prescribed in the DP Regulations.

- The depositories shall report to SEBI about the approval as stated above on a monthly basis.
- The participant shall apply to SEBI for permanent registration through any of the depositories in which it is acting as a participant as per the DP Regulations.
- The depositories shall coordinate and share information with each other, about their participants.

SARAL ACCOUNT OPENING FORM FOR RESIDENT INDIVIDUALS

SEBI vide circular dated March 04, 2015 provided for SARAL account opening for resident individuals. An individual investors can open a trading account and demat account by filling up a simplified Account Opening Form ('AOF') termed as 'SARAL AOF' and will also have the option to obtain other facilities, whenever they require, on furnishing of additional information as per prescribed regulations/circulars.

For these set of individual investors, the requirement of submission of 'proof of address' is as follows:

- Individual investor may submit only one documentary proof of address (either residence/correspondence or permanent) while opening a trading account and / or demat account or while undergoing updation.
- In case the proof of address furnished by the said investor is not the address where the investor is currently residing, the intermediary may take a declaration of the residence/correspondence address on which all correspondence will be made by the intermediary with the investor. No proof is required to be submitted for such correspondence/residence address.
- In the event of change of address due to relocation or any other reason, investor may intimate the new address for correspondence to the intermediary within two weeks of such a change. The residence/correspondence address and any such change thereof may be verified by the intermediary through 'positive confirmation' such as (i) acknowledgment of receipt Welcome Kit/ dispatch of contract notes / any periodical statement, etc. (ii) telephonic conversation; (iii) visits, etc.

LESSON ROUND UP

- The legal framework for depository system in the Depositories Act, 1996 provides for the establishment of single or multiple depositories.
- There are two Depositories functioning in India, namely the National Securities Depository Limited (NSDL) and the Central Depository Services (India) Limited (CDSL).
- All the securities held by a depository are dematerialized and are in a fungible form.
- In the depository system, the ownership and transfer of securities takes place by means of electronic book entries.
- A Depository Participant (DP) is the representative (agent) of the investor in the depository system providing the link between the Company and investor through the Depository.
- The Depository Act, 1996 and SEBI (Depositories and Participants) Regulations, 1996 regulates the function of Depositories and participants.
- Regulation 55A of SEBI (Depositories and Participants) Regulations, 1996 provides that every issuer shall submit audit report on a quarterly basis to the concerned stock exchanges audited by a practicing Company Secretary or a qualified Chartered Accountant, for the purposes of reconciliation of the total issued capital, listed capital and capital held by depositories in dematerialized form, the details of changes in share capital during the quarter and the in-principle approval obtained by the issuer from all the stock exchanges where it is listed in respect of such further issued capital.

- Both the Depositories in India have allowed Practising Company Secretaries to undertake internal audit of the operations of Depository Participants (DPs).
- Depository Participants are subject to concurrent audit by a Practising Company Secretary or qualified Chartered Accountant. Concurrent Audit includes audit of process of demat account opening, control and verification of delivery instruction slips.

GLOSSARY

Beneficial owner (BO)	The true owner of a security or property, which may be registered in another name. Means a person whose name appears as such on the records of the depository.
ISIN	International Securities Identification Number (ISIN) is a code that uniquely identifies a specific security, which is allocated at the time of admitting the same in the depository system.
Joint Account	It means a bank or a demat account in the names of more than one person (maximum three in case of a demat account). All the account holders must give their signature to operate a demat account held jointly.
Pledge	Any person having a demat account can pledge securities against loan / credit facilities extended by a pledgee, who too has a demat account with a DP.
RRN	A system generated unique number when a remat request is set up.
Transmission	Transmission of securities denotes a process by which ownership of securities is transferred to a legal heir or to some other person by operation of law. In case of transmission transfer deed and stamp duty are not required.

SELF TEST QUESTIONS

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation.)

1. Briefly outline the concept of Depository system in India.
2. Enumerate the enquiry, inspection and penalties under the Depositories Act, 1996.
3. Explain in detail the power of depositories to make bye-laws under the Depositories Act, 1996.
4. Give an overview of the rights and obligations of Depositories, Participants and issuers under SEBI (Depositories and Participants) Regulations, 1996.
5. Explain in detail the Statement required to be sent to the beneficial owner by a DP under BSDA facility?
6. Write short note on:
 - (a) Dematerialisation charges.
 - (b) Models of Depository.
 - (c) Internal Audit of Depository Participants.
 - (d) Concurrent Audit.
 - (e) Single registration for depository participants.

Lesson 19

Listing and Delisting of Securities

LESSON OUTLINE

- Introduction
- Types of Listing
- Benefits of Listing
- Legal Provision on Listing
- Compliances under SEBI (Listing Obligation and Disclosure Requirements) Regulations, 2015
- Corporate Governance
- Corporate Governance under SEBI (LODR), 2015
- Corporate Governance – Listing Regulations vis-a-vis Companies Act, 2013
- Delisting
- SEBI (Delisting of Equity Shares) Regulations, 2009
- Voluntary Delisting
- Delisting from only some of the recognised stock exchanges
- Procedure for Delisting
- Special provisions for small companies and delisting by operation of law
- Compulsory delisting
- Schedule III
- LESSON ROUND-UP
- GLOSSARY
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

The prime objective of admission of securities to dealings on the Stock Exchange is to provide liquidity and marketability and also to provide a mechanism for effective management of trading. Thus, listing is the admission of securities to dealings on a recognized stock exchange. For a company to be listed on a stock exchange, the company has to enter into a listing agreement with the respective stock exchange(s). Listing agreement provides conditions to be complied with including the norms for better corporate Governance. Listing agreement also work as a link between the company and investor because it requires the company to provide basic information to the shareholder and grievance redressal mechanism. Further, a company can delist its securities from the stock exchange.

This lesson will enable the students to have conceptual understanding of Listing of Securities and various clauses of Listing Agreement and Corporate Governance under SEBI (LODR), 2015 and delisting of securities etc.

INTRODUCTION

Listing of securities with stock exchange is a matter of great importance for companies and investors, because this provides the liquidity to the securities in the market. Any company offering its shares to the public for subscription is required to be listed on the stock exchange and has to comply with the conditions as provided in the SEBI (ICDR) Regulations, 2009. According to the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009, [(SEBI (ICDR) Regulations, 2009)], a company has to file a draft offer document along with prescribed fees to SEBI through the lead merchant banker, at least thirty days prior to registering the prospectus with the Registrar of Companies. The company has to obtain in-principle approval from recognised stock exchanges in which the company proposes to get its securities listed. A company is required to complete the allotment of securities offered to the public and/or refund the application moneys within fifteen days from the date of closure of the issue.

In addition, a company intending to have its share listed has to comply with the listing requirements prescribed by the Stock Exchange. A company seeking listing of their securities on the Stock Exchange is required to enter into a formal listing agreement with the Stock Exchange. SEBI has prescribed and also specified all the quantitative and qualitative requirements to be continuously complied with by the issuer for continued listing. The Stock Exchange monitors such compliance and companies who do not comply with the provisions of the listing agreement may be suspended from trading on the Stock Exchange.

Only public companies are allowed to list their securities in the stock exchange. Private Limited companies cannot get listing facility. They should first convert themselves into public limited companies and their Articles of Association should also contain prohibitions as laid down in the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 ('LODR Regulations') and as applicable to public limited companies.

TYPES OF LISTING

Listing of securities falls under 5 groups –

Initial Listing

If the shares or securities are to be listed for the first time by a company on a stock exchange is called initial listing.

Listing for Public Issue

When a company whose shares are listed on a stock exchange comes out with a public issue of securities, it has to list such issue with the stock exchange.

Listing for Rights Issue

When companies whose securities are listed on the stock exchange issue securities to existing shareholders on rights basis, it has to list such rights issues on the concerned stock exchange.

Listing of Bonus Shares

Shares issued as a result of capitalisation of profit through bonus issue shall list such issues also on the concerned stock exchange.

Listing for merger or amalgamation

When new shares are issued by an amalgamated company to the shareholders of the amalgamating company, such shares are also required to be listed on the concerned stock exchange.

BENEFITS OF LISTING

The following benefits are available when securities are listed by a company in the stock exchange–

- (1) Public image of the company is enhanced.
- (2) The liquidity of the security is ensured making it easy to buy and sell the securities in the stock exchange.
- (3) Tax concessions are made available both to the investors and the companies.
- (4) Listing procedure compels company management to disclose important information to the investors enabling them to make crucial decisions with regard to keeping or disposing of such securities.
- (5) Listed companies command better support such as loans and investments from Banks and FIs.

LEGAL PROVISION ON LISTING

According to Section 40(1) of the Companies Act 2013, every company which intends to make public offer of securities should make an application to one or more recognised stock exchanges before making such offer. Sub section 2 of this Section provides that the company shall state the name of the stock exchanges on which its securities will be dealt with.

Section 24 of the Companies Act, 2013 provides that, any company which is listed or intend to get their securities listed on any recognised stock exchange will be administered by regulation prepared by SEBI for matters relating to issue and transfer of securities and non payment of dividend.

As per Section 4 of the Securities Contracts (Regulation) Act, 1956, every recognised stock exchange has the powers to make bye-laws for the listing of securities on the stock exchange, inclusion of any security for the purpose of dealings and suspension or withdrawal of securities and the prohibition of trading in any specified security, subject to SEBI approval.

Every company while submitting its application for listing with the stock exchange(s) should produce a number of documents as enclosures to satisfy the requirements of the concerned stock exchange. It should also give a number of undertakings as a condition precedent before listing as sought by the concerned stock exchange. Finally when the stock exchange(s) agree(s) to list the securities, the company shall execute a listing agreement with the stock exchange(s).

When a company signs a listing agreement with a stock exchange, it means it has entered into a legally binding contract with that stock exchange and it has to ensure compliance of each and every term and condition of the listing agreement. For failure to ensure such compliance the stock exchange can take an action against the company after giving an opportunity of being heard.

Listing of Securities on Indian Stock Exchanges, thus, is governed by the provisions in the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, Companies Act, 2013, the Securities Contracts (Regulation) Act, 1956, the Securities Contracts (Regulation) Rules, 1957, Rules, bye laws, regulations of concerned stock exchange and circulars/guidelines issued by the Central Government and SEBI.

COMPLIANCES UNDER SEBI (LISTING OBLIGATIONS AND DISCLOSURE REQUIREMENTS) REGULATIONS, 2015

SEBI has notified SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 ("Listing Regulations") on September 2, 2015 after following the consultation process. The Listing Regulations came into force w.e.f. 01 December 2015.

Framework

The broad framework of Listing Regulations are outlined as follows:

The Listing Regulations have been sub-divided into two parts viz.

- (i) Substantive provisions incorporated in the main body of Regulations; and
- (ii) Procedural requirements in the form of Schedules to the Regulations.

The Regulations are consisting of XII chapters and X schedules.

- Chapter I is consisting of Definition part.
- Chapter II of the SEBI Listing Regulations provide the broad principles in relation to disclosures and obligations of the listed entities. In the event of absence of specific requirements or ambiguity, these principles would serve to guide the listed entities.
- Chapter III of the SEBI Listing Regulations specifies common obligations of all listed entities. These include:
 - General obligation of compliance of listed entity,
 - Appointment of common compliance officer and his obligations,
 - Appointment of Share Transfer Agent or management of share transfer facility in-house
 - Co-operation with intermediaries registered with SEBI and submission of correct and adequate information within the specified timelines and procedures
 - Preservation of documents – permanent and for 8 years
 - Filings on electronic platform
 - Payment of dividend or interest or redemption or repayment through RBI approved electronic mode
 - Grievance Redressal mechanism
 - Mandatory registration on SCORES to handle investor complaints electronically
 - Quarterly reporting of investor complaints to the Board of directors and recognized stock exchange.
- Chapter IV to IX of the SEBI Listing Regulations deal with obligations which are applicable to specific types of securities have been incorporated in various chapters.
- Chapter X and XI of the SEBI Listing Regulations list down the responsibilities of the stock exchanges to monitor compliance or adequacy / accuracy of compliance with the provisions of these regulations and to take action for non-compliance.
- Chapter XII containing miscellaneous provisions.

Applicability

Unless otherwise provided, these regulations shall apply to the listed entity who has listed any of the following designated securities on recognised stock exchange(s):

- (a) specified securities listed on main board or SME Exchange or institutional trading platform;
- (b) non-convertible debt securities, non-convertible redeemable preference shares, perpetual debt instrument, perpetual non-cumulative preference shares;
- (c) Indian depository receipts;
- (d) securitised debt instruments;
- (e) units issued by mutual funds;

- (f) any other securities as may be specified by SEBI.

Company desirous of listing its securities shall enter into a listing agreement with the stock exchange. Existing listed entities are required to execute a fresh listing agreement within 6 months from date of notification of SEBI Listing Regulations.

According to Section 2 (52) of the Companies Act, 2013, listed company means a company which has any of its securities listed on any recognised stock exchange. This means that if a private limited company has its debt securities listed on any recognised stock exchange, then such company is under the ambit of listed company category for complying with the Companies Act, 2013 and rules and regulation made thereunder.

According to SEBI (LODR) Regulations, 2015 “listed entity” means an entity which has listed, on a recognised stock exchange(s), the designated securities issued by it or designated securities issued under schemes managed by it, in accordance with the listing agreement entered into between the entity and the recognised stock exchange(s).

Integrated Report

According to Regulation 4(1) (d) of SEBI LODR states “the listed entity shall provide adequate and timely information to recognised stock exchange(s) and investors”. In this regard, the International Integrated Reporting Council (IIRC) has prescribed Guiding Principles which support the preparation of an integrated report.

In order to improve disclosure standards, the listed entities are advised to adhere to the following:

- a. Integrated Reporting may be adopted on a voluntary basis from the financial year 2017-18 by top 500 companies which are required to prepare BRR.
- b. The information related to Integrated Reporting may be provided in the annual report separately or by incorporating in Management Discussion & Analysis or by preparing a separate report (annual report prepared as per IR framework).
- c. In case the company has already provided the relevant information in any other report prepared in accordance with national/international requirement / framework, it may provide appropriate reference to the same in its Integrated Report so as to avoid duplication of information.
- d. As a green initiative, the companies may host the Integrated Report on their website and provide appropriate reference to the same in their Annual Report.

REQUIREMENTS BEFORE THE SCHEME OF ARRANGEMENT IS SUBMITTED FOR SANCTION BY THE NATIONAL COMPANY LAW TRIBUNAL (NCLT)

According to Regulation 37 of SEBI (LODR), 2015 provides that the listed entities desirous of undertaking scheme of arrangement or involved in a scheme of arrangement shall file the draft scheme with Stock Exchange(s) for obtaining Observation Letter or No- objection Letter, before filing such scheme with any court or Tribunal.

A. REQUIREMENTS TO BE FULFILLED BY LISTED ENTITY

1. **Designated Stock Exchange:** Listed entities shall choose one of the Stock Exchanges having nationwide trading terminals as the designated Stock Exchange for the purpose of coordinating with SEBI.

2. Submission of Documents

The Listed entity shall submit the following documents to the Stock Exchanges:-

- (a) Draft Scheme of arrangement/ amalgamation/ merger/ reconstruction/ reduction of capital, etc.
- (b) Valuation Report;
- (c) Report from the Audit Committee recommending the Draft Scheme, taking into consideration, *inter alia*, the Valuation Report. The Valuation Report is required to be placed before the Audit Committee of the listed entity;

- (d) Fairness opinion by a SEBI Registered merchant banker on valuation of assets / shares done by the valuer for the listed entity and unlisted entity;
- (e) Pre and post amalgamation shareholding pattern of unlisted entity;
- (f) Audited financials of last 3 years (financials not being more than 6 months old) of unlisted entity;
- (g) Auditor's Certificate;
- (h) Detailed Compliance Report as per the format specified by SEBI duly certified by the Company Secretary, Chief Financial Officer and the Managing Director, confirming compliance with various regulatory requirements specified for schemes of arrangement and all accounting standards.

3. Conditions for schemes of arrangement involving unlisted entities

In case of schemes of arrangement between listed and unlisted entities, the following conditions shall be satisfied:

- (a) The listed entity shall include the applicable information pertaining to the unlisted entity/ies involved in the scheme in the format specified for abridged prospectus as provided in Part D of Schedule VIII of the ICDR Regulations, in the explanatory statement or notice or proposal accompanying resolution to be passed sent to the shareholders while seeking approval of the scheme.

The accuracy and adequacy of such disclosures shall be certified by a SEBI Registered Merchant Banker after following the due diligence process. Such disclosures shall also be submitted to the Stock Exchanges for uploading on their websites.
- (b) The percentage of shareholding of pre-scheme public shareholders of the listed entity and the Qualified Institutional Buyers (QIBs) of the unlisted entity, in the post scheme shareholding pattern of the "merged" company shall not be less than 25%.
- (c) Unlisted entities can be merged with a listed entity only if the listed entity is listed on a Stock Exchange having nationwide trading terminals.

4. Valuation Report: All listed entities are required to submit a valuation report from an Independent Chartered Accountant. However, Valuation Report is not required in cases where there is no change in the shareholding pattern of the listed entity/resultant company.

'Change in the Shareholding Pattern' means:

- (i) change in the proportion of shareholding of any of the existing shareholders of the listed entity in the resultant company; or
- (ii) new shareholder being allotted equity shares of the resultant company; or
- (iii) existing shareholder exiting the company pursuant to the Scheme of Arrangement

'Resultant Company' means a company arising / remaining after the listed entity undertakes a Scheme of Arrangement.

5. Auditor's certificate: An auditors' certificate shall be filed to the effect that the accounting treatment contained in the scheme is in compliance with all the Accounting Standards specified by the Central Government under Section 133 of the Companies Act, 2013 read with the rules framed thereunder or the Accounting Standards issued by ICAI, as applicable, and other generally accepted accounting principles.

However, in case of companies where the respective sectoral regulatory authorities have prescribed norms for accounting treatment of items in the financial statements contained in the scheme, the requirements of the regulatory authorities shall prevail.

Explanation – For this purpose, mere disclosure of deviations in accounting treatments as prescribed in the aforementioned Accounting Standards and other generally accepted Accounting Principles shall not be deemed as compliance with the above.

6. Redressal of Complaints: The Listed entity shall submit to Stock Exchanges a 'Report on Complaints' which

shall contain the details of complaints/comments received by it on the Draft Scheme from various sources (complaints/comments written directly to the listed entity or forwarded to it by the Stock Exchanges/SEBI) prior to obtaining Observation Letter from Stock Exchanges on Draft Scheme. The Report shall be submitted within 7 days of expiry of 21 days from the date of filing of Draft Scheme with Stock Exchanges and hosting the Draft Scheme along with documents specified above on the websites of Stock Exchanges and the listed entity.

7. Disclosure on the Website: Immediately upon filing of the Draft Scheme of arrangement with the Stock Exchanges, the listed entity shall disclose the Draft Scheme of arrangement and all the documents on its website. The Listed entity shall also disclose the Observation Letter of the Stock Exchanges on its website within 24 hours of receiving the same.

8. Explanatory Statement or notice or proposal accompanying resolution sent to shareholders for seeking approval of scheme

The Listed entity shall include the Observation Letter of the Stock Exchanges, in the explanatory statement or notice or proposal accompanying resolution to be passed sent to the shareholders seeking approval of the Scheme.

The listed entity shall ensure that in the explanatory statement or notice or proposal accompanying resolution to be passed, it shall disclose the pre and post-arrangement or amalgamation, expected capital structure and shareholding pattern, and the “fairness opinion” obtained from a merchant bankers on valuation of assets / shares done by the independent chartered accountant for the listed entity and unlisted entity.

9. Approval of Shareholders to Scheme through e- Voting: The Listed entities shall ensure that the Scheme of Arrangement submitted with the NCLT for sanction, provides for voting by public shareholders through e-voting, after disclosure of all material facts in the explanatory statement sent to the shareholders in relation to such resolution.

B. OBLIGATIONS OF STOCK EXCHANGE(S)

The designated Stock Exchange, upon receipt of the Draft Scheme of Arrangement and documents mentioned above shall forward the same to SEBI within three working days.

The Stock Exchanges where the specified securities are listed / proposed to be listed shall also disclose on their websites. It shall also disclose the Observation Letter on its website immediately upon issuance.

C. PROCESSING OF THE DRAFT SCHEME BY SEBI

Upon receipt of Observation Letter’ or ‘No-Objection’ letter from the Stock Exchanges, SEBI shall provide its comments on the Draft Scheme of arrangement to the Stock Exchanges.

While processing the Draft Scheme, SEBI may seek clarifications from any person relevant in this regard including the listed entity or the Stock Exchanges and may also seek an opinion from an Independent Chartered Accountant.

SEBI shall endeavour to provide its comments on the Draft Scheme to the stock exchanges within 30 days from the later of the following:

- (a) date of receipt of satisfactory reply on clarifications, if any sought from the listed entity by SEBI; or
- (b) date of receipt of opinion from Independent Chartered Accountant, if sought by SEBI; or
- (c) date of receipt of Observation Letter’ or ‘No-Objection’ letter from the Stock Exchanges.
- (d) date of receipt of copy of in-principle approval for listing of equity shares of the company seeking exemption from Rule 19(2)(b) of Securities Contracts (Regulation) Rules, 1957 on designated Stock Exchange, in case the listed entity is listed solely on regional Stock Exchange.

All complaints/comments received by SEBI on the Draft Scheme of arrangement shall be forwarded to the designated Stock Exchange, for necessary action and resolution by the listed entity.

II. REQUIREMENTS AFTER THE SCHEME IS SANCTIONED BY THE HON'BLE HIGH COURT / NCLT (HEREINAFTER REFERRED TO AS "APPROVED SCHEME")

Upon sanction of the Scheme by the Hon'ble High Court / NCLT, the listed entity shall submit the documents mentioned below to the Stock Exchanges:-

- (a) Copy of the High Court/ NCLT approved Scheme;
- (b) Result of voting by shareholders for approving the Scheme;
- (c) Statement explaining changes, if any, and reasons for such changes carried out in the Approved Scheme of arrangement vis-a-vis the Draft Scheme of arrangement;
- (d) Status of compliance with the Observation Letter or No Objection Letter of the Stock Exchange(s);
- (e) The application seeking exemption from Rule 19(2)(b) of SCRR, 1957, wherever applicable; and
- (f) Report on Complaints.

Sl. No.	Regulation No	Subject	Particulars
Common Obligations of Listed Entities			
1.	Regulation 5	General obligation of compliance	To ensure that key managerial personnel, directors, promoters or any other person dealing with the listed entity, complies with responsibilities or obligations, if any, assigned to them under these regulations
2.	Regulation 6	Appointment of Compliance Officer	To appoint a qualified company secretary as the compliance officer.
3.	Regulation 7(1)	Appointment of Share Transfer Agent	The company can manage in house Share Transfer Facility. But <i>As and When the Total Number of Holders of Securities of the Listed Entity exceeds 1,00,000/-</i> .
4.	Regulation 7(3)	Submission a Compliance Certificate to the Exchange	The Listed entity shall submit a Compliance Certificate to the Exchange duly <i>signed by both</i> Compliance Officer and Authorised Representative of the Share Transfer Agent, wherever applicable, <i>within 1 month of end of each half of the financial year.</i>
5.	Regulation 7(4)	Alteration in Share Transfer Agent	Any change or appointment of a new Share Transfer Agent, the listed entity shall enter into a TRIPARTITE AGREEMENT <i>between Listed entity, Existing and New Share Transfer Agent.</i>
6.	Regulation 7(5)	Intimation to Stock Exchange	The Listed Entity shall intimate the appointment of Share Transfer Agent <i>within 7 days on entering into agreement.</i>
7.	Proviso of Regulation 7	Non- Applicability of provisions of Compliance Officer	The requirement of this regulation shall not applicable in case of units issued by Mutual Funds which are listed on Recognized Stock exchange.

8.	Regulation 8	Co-operation with intermediaries registered with SEBI	shall <i>Co-operate with and submit correct and adequate information</i> to the intermediaries registered with SEBI such as credit rating agencies, registrar to an issue and Share Transfer agents, Debenture Trustee etc., within timelines and procedures specified under the Act, Regulations and Circulars issued there under.
9.	Regulation 9	Preservation of documents	<p>The listed entity shall have a POLICY for preservation of documents, approved by its board of directors. The Company will classifying them in <i>at least two categories</i> as follows –</p> <ul style="list-style-type: none"> – Documents whose preservation shall be <i>Permanent In Nature</i> ; – Documents with preservation period of <i>NOT LESS THAN EIGHT YEARS after completion of the relevant transaction.</i>
10.	Regulation 10	Filing of Information	The listed entity shall file the reports, statements, documents, filings and any other information with the recognized stock exchange(s) <i>on the Electronic Platform</i> as specified by SEBI or the recognized stock exchange(s).
11.	Regulation 11	Applicability of Scheme of Arrangement	The listed entity shall ensure that any scheme of arrangement/amalgamation /merger/ reconstruction /reduction of capital etc. to be presented to any Court or Tribunal does not in any way violate, override or limit the provisions of securities laws or requirements of the stock exchange(s).
12.	Regulation 12	Payment of dividend or interest or redemption or repayment	<p>The listed entity shall use any of the electronic mode of payment facility approved by the RBI, in the manner specified in Schedule I, for the payment of the following:</p> <ul style="list-style-type: none"> (i) Payment of dividend or interest or redemption or repayment (ii) Dividend (iii) Interest (iv) Redemption or Repayment of amounts <p><i>Modes of Payment if electronic mode is not possible</i> then payment can be made by following:</p>

			(i) 'Payable-at-Par' Warrants (ii) Cheques
13.	Regulation 13	Grievance Redressal Mechanism	<p>The listed entity shall ensure that Adequate Steps Are Taken for expeditious redressal of investor complaints. The listed entity shall file with the recognized stock exchange(s) on a QUARTERLY BASIS,</p> <ul style="list-style-type: none"> - a statement giving <ul style="list-style-type: none"> • The number of investor complaints pending at the beginning of the quarter, • Those received during the quarter, • Disposed of during the quarter and • Those remaining unresolved at the end of the quarter. - within 21 days from the end of each quarter,
14.	Regulation 14	Fees and other Charges to be paid to the Recognised Stock Exchange(s)	The listed entity shall pay all such fees or charges, as applicable, to the recognized stock exchange(s), in the manner specified by SEBI or the recognized stock exchange(s).
Common Obligations of Listed Entities which has listed its Specified Securities			
1.	Regulation 15(1)	Applicability	<p>The provisions of this chapter shall apply to following Listed Entities, which has listed with any recognize Stock Exchange (s) for its specified securities either on:</p> <ul style="list-style-type: none"> • Main Board; or • SME Exchange; or • Institutional Trading Platform.
2.	Regulation 15 (2)	Non- Applicability	<ul style="list-style-type: none"> – Listed entities having paid up equity share capital not exceeding Rs. 10 crore and net worth not exceeding Rs. 25 crore, as on the last day of the previous financial year. – Listed entities which have listed its specified securities on the SME Exchange – Listed Entities which are not companies, but body Corporate or are subject to regulations under other statues shall not apply to the extent that it does not violate their respective statutes and guidelines

			<p>or directives issued by the relevant authorities.</p> <p>If any time Listed Company cross the above given limits, then such listed entity shall comply with the requirements those regulations within six months from the date on which the provisions became applicable to the listed entity.</p>
3.	Regulation 22	Vigil Mechanism	<p>The listed entity shall formulate a vigil mechanism for directors and employees to report genuine concerns.</p> <p>The vigil mechanism shall provide for adequate safeguards against victimization of director(s) or employee(s) or any other person who avail the mechanism.</p> <p>The Vigil Mechanism also provides for direct access to the chairperson of the audit committee in appropriate or exceptional cases.</p>
4.	Regulation 28	In-principle approval of recognized stock exchange(s)	<ul style="list-style-type: none"> The listed entity, before issuing securities, shall obtain an 'in-principle' approval from recognised stock exchange(s) in the following manner : <ul style="list-style-type: none"> – where the securities are listed only on recognised stock exchange (s) having nationwide trading terminals, from all such stock exchange (s); – where the securities are not listed on any recognised stock exchange having nationwide trading terminals, from all the stock exchange(s) in which the securities of the issuer are proposed to be listed; – where the securities are listed on recognised stock exchange(s) having nationwide trading terminals as well as on the recognised stock exchange(s) not having nationwide trading terminals, from all recognised stock exchange(s) having nationwide trading terminals. This regulation shall not be applicable for securities issued pursuant to the Scheme

			of Arrangement for which the listed entity has already obtained No Objection letter from recognized stock exchange(s) in accordance with regulation 37.
5.	Regulation 29(1)(a) & 29(2)	Prior Intimation to Stock exchange about Board Meeting	The listed entity shall give prior intimation to stock exchange about the meeting of the board of directors in which the financial results viz., quarterly, half-yearly, or annual, as the case may be, at least 5 working days in advance excluding the date of the intimation and date of meeting.
6.	Regulation 29(1)(b) to 29(1)(f) & 29(2)	Prior Intimation to Stock exchange about Board Meeting	<p>The listed entity shall give prior intimation to stock exchange about the meeting of the board of directors in which the following proposals is to be considered: -</p> <ul style="list-style-type: none"> – buy-back of securities – voluntary delisting – fund raising by way of FPO, rights issue, QIP, debt issue, ADR/GDR/FCCB, preferential issue or any other method and for determination of issue price – Declaration/recommendation of dividend, issue of convertible securities including convertible debentures or of debentures carrying a right to subscribe to equity shares or the passing over of dividend – Declaration of bonus securities where such proposal is communicated to the board of directors of the listed entity as part of the agenda papers. <p>Such intimation shall be given, at least 2 working days in advance, excluding the date of the intimation and date of meeting.</p>
7.	Regulation 29(3)	Prior Intimation to Stock exchange about Board Meeting	<p>The listed entity shall give intimation to the stock exchange(s) at least eleven working days before any of the following proposal is placed before the board of directors</p> <ul style="list-style-type: none"> – any alteration in the form or nature of any of its securities that are listed on the stock exchange or in the rights or privileges of the holders thereof. – any alteration in the date on which, the

			interest on debentures or bonds, or the redemption amount of redeemable shares or of debentures or bonds, shall be payable.
8.	Regulation 30(6)	<p>Disclosure of events or information:-</p> <ul style="list-style-type: none"> – Disclosure of Material Event – Materiality – Criteria for Determination of Materiality of Events Information – Authorization to KMP 	<ul style="list-style-type: none"> - Every Listed Entity shall make disclosures of any events or information, which, in the opinion of the board of directors of the listed company, is material. – SEBI has also decided that every listed entity shall also make disclosures with respect to loan from banks and financial institutions – Materiality : – Events specified in Para A of Part A of Schedule III are deemed to be Material. – Events specified in Para B of Part A of Schedule III are deemed to be Material Event, if guidelines of materiality APPLICABLE, guidelines given in sub-regulation 4 of regulation 30. – Formation of policy for determination of materiality shall be based on following criteria : <ul style="list-style-type: none"> (a) the omission of an event or information, which is likely to result in discontinuity or alteration of event or information already available publicly; or (b) the omission of an event or information is likely to result in significant market reaction if the said omission came to light at a later date; (c) In case where the criteria specified in sub-clauses (a) and (b) are not applicable, an event/information may be treated as being material if in the opinion of the board of directors of listed entity, the event / information is considered material, – The board of directors of the listed entity shall authorize one or more Key

		<ul style="list-style-type: none"> – Intimation to Stock Exchange – Continuation of Disclosure to Stock Exchange – Disclosure on Website – Disclosure relating to Materiality of Subsidiary 	<p>Managerial Personnel for the purpose of:</p> <ul style="list-style-type: none"> – Determining materiality of an event; or – Determining materiality of an information; or – Making disclosure to Stock Exchange(s) <ul style="list-style-type: none"> – Disclose to the stock exchange(s) of all events, as specified in Part A [Part A includes Para A & Para B] of Schedule III, or information as soon as reasonably possible and not later than 24 hours of occurrence of event or information. <p><i>In case disclosure made after 24 hours of occurrence of event or information, along with disclosure provide explanation for delay.</i></p> <ul style="list-style-type: none"> – The listed entity shall, with respect to disclosures referred to in this regulation, make disclosures updating material developments on a regular basis, till such time the event is resolved/ closed, with relevant explanations. – The listed entity shall disclose all such events or information, which has been, disclosed to stock exchange(s), on its website and give continuous such disclosures on the website of the listed entity for a minimum period of five years and thereafter as per the archival policy of the listed entity, as disclosed on its website. – The listed entity shall disclose all events or information with respect to subsidiaries which are material for the listed entity to both Stock Exchange and on Website. <p>Note :-</p> <ul style="list-style-type: none"> – The listed entity shall provide specific and adequate reply to all queries raised by stock exchange(s) with respect to any events or information. – In case where an event occurs or an information is available with the listed entity, which has not been indicated in Para A or B of Part A of Schedule III, but
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			which may have material effect on it, the listed entity is required to make adequate disclosures in regard thereof.
9.	Regulation 31	Holding of specified securities and shareholding pattern	<ul style="list-style-type: none"> The listed entity shall submit to the stock exchange(s) a statement showing Holding of securities & Shareholding Pattern separately for each class of securities:- <ul style="list-style-type: none"> In case of listing of its securities, 1 day prior to listing of its securities. In case of Quarterly basis, within 21 days from the end of each quarter. In case of any capital restructuring resulting in a change exceeding 2% of the total paid up share capital, within 10 days of capital restructuring. 100% shareholding of promoter and promoter group shall be in demat form. Listed entity shall comply with circulars or directions issued with respect to maintenance of shareholding in demat form.
10.	Regulation 31A	Disclosure of Class of shareholders and Conditions for Reclassification	The event of re-classification shall be disclosed to the stock exchanges as a material event within 24 hours of occurrence of the event.
11.	Regulation 32	Statement of deviation(s) or variation(s)	<p>A listed entity shall submit to the stock exchange the following statement(s) on a quarterly basis for public issue, rights issue, preferential issue etc. :-</p> <ul style="list-style-type: none"> indicating deviations, if any, in the use of proceeds from the objects stated in the offer document or explanatory statement to the notice for the general meeting, as applicable; indicating category wise variation (capital expenditure, sales and marketing, working capital etc.) between projected utilisation of funds made by it in its offer document or explanatory statement to the notice for the general meeting, as applicable and the actual utilisation of funds.

12.	Regulation 33	Financial Results	<ul style="list-style-type: none"> • The listed entity or its subsidiaries shall submit quarterly and year-to-date standalone financial results to the stock exchange <i>within 45 days of end of each quarter</i>, other than the last quarter. • Unaudited financial result shall be accompanied by Limited Review Report. Audited financial results accompanied by audit report. • FR shall be signed by the chairperson or managing director, or a whole time director or in the absence of all of them; it shall be signed by any other director of the listed entity who is duly authorized by the BOD to sign the FR. <p>While placing the financial results before the board of directors, the chief executive officer and chief financial officer of the listed entity shall certify that the financial results do not contain any false or misleading statement or figures and do not omit any material fact which may make the statements or figures contained therein misleading.</p> <ul style="list-style-type: none"> • The listed entity shall submit with stock exchange <i>within 60 days from the end of the financial year</i>, annual audited standalone financial results for the financial year along with the audit report or in case entity having subsidiaries it shall, while submitting annual audited standalone financial results also submit annual audited consolidated financial results along with the audit report and Statement on Impact of Audit Qualifications, applicable only for audit report with modified opinion and the listed entity shall also submit the audited financial results in respect of the last quarter along-with the results for the entire financial year. <p>Further that, in case of audit reports with unmodified opinion(s), the listed entity shall furnish a declaration to that effect to the stock exchange(s) while publishing the annual audited financial results.</p>
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			<ul style="list-style-type: none"> The listed entity shall also submit as part of its standalone or consolidated financial results for the half year, by way of a note, a statement of assets and liabilities as at the end of the half-year. <p>Publishing in newspaper and on website of the company.</p> <p><i>[Financial Results shall be published within 48 hours of conclusion of Board Meeting in at least one English Language national daily newspaper circulating in the whole or substantially the whole of India and in one daily newspaper published in the language of the region, where the registered office of the listed entity is situated as well also put on website of the company]</i></p>
13.	Regulation 34	Annual Report	<p>A listed entity shall submit the annual report to the stock exchange within 21 working days of it being approved and adopted in the Annual General Meeting as per provisions of Companies Act, 2013. The annual report shall contain the following:</p> <ul style="list-style-type: none"> (a) audited financial statements i.e. balance sheets, profit and loss accounts etc; and statement on Impact of audit qualifications as stipulated in Regulation 33 (b) consolidated financial statements audited by its statutory auditors; (c) cash flow statement presented only under the indirect method as prescribed in Accounting Standard-3 or Indian Accounting Standard 7, as applicable, specified in Section 133 of the Companies Act, 2013 read with relevant rules framed thereunder or as specified by ICAI, whichever is applicable; (d) directors report; (e) management discussion and analysis report - either as a part of directors report or addition thereto; (f) for the top five hundred listed entities based on market capitalization (calculated as on March 31 of every financial year), business responsibility report.

14.	Regulation 35	Annual Information Memorandum	Listed entity shall submit to the stock exchanges an Annual Information Memorandum in the manner specified by SEBI from time to time.
15.	Regulation 36	Documents & information to shareholders	<p>The Listed Entity shall send Annual report to the holders of securities, not less than 21 days before the AGM in the following manner :-</p> <ul style="list-style-type: none"> • Soft copies of full annual report to all those shareholders who have registered their e-mail addresses. • Hard copy containing salient features to those who have not registered their e-mail addresses. • Hard copies of full annual reports to all those who request for the same.
16.	Regulation 37	Draft Scheme of Arrangement & Scheme of Arrangement	<ul style="list-style-type: none"> • Before filing the draft scheme of arrangement before any Court or Tribunal, it shall be filed with the stock exchanges. • An observation letter or no-objection letter shall be obtained before filing such draft scheme. • Such observation letter or no-objection letter shall be placed before the Court or Tribunal at the time of seeking approval of the scheme of arrangement. • The observation or no-objection letter shall be valid for a period of 6 Months from the date of issuance within which the draft scheme of arrangement shall be submitted to the Court or Tribunal. • Upon sanction of the Scheme by the Court or Tribunal the listed entity shall submit such prescribed documents to the stock exchanges. • Nothing contained in this regulation shall apply to draft schemes which solely provide for merger of a wholly owned subsidiary with its holding company. However, such draft schemes shall be filed with the stock exchanges for the purpose of disclosures.
17.	Regulation 38	Minimum Public Shareholding	The listed entity shall comply with the minimum public shareholding requirements specified in Rule 19(2) and Rule 19A of the

			Securities Contracts (Regulation) Rules, 1957 in the manner as specified by SEBI from time to time. However, the provisions of this regulation shall not apply to entities listed on institutional trading platform without making a public issue.
18.	Regulation 39	Issuance of Certificates or Receipts/Letters/Advices for securities and dealing with unclaimed securities	<p>The listed entity shall:</p> <ul style="list-style-type: none"> • issue certificates or receipts or advices, as applicable, of subdivision, split, consolidation, renewal, exchanges, endorsements, issuance of duplicates thereof or issuance of new certificates or receipts or advices, as applicable, in case of loss or old decrepit or worn out certificates or receipts or advices, as applicable <i>within a period of thirty days from the date of such lodgement.</i> • Submit information regarding loss of share certificates and issue of the duplicate certificates, to the stock exchange <i>within two days of its getting information.</i> • Comply with the procedural requirements specified in Schedule VI while dealing with securities issued pursuant to the public issue or any other issue, physical or otherwise, which remain unclaimed and/or are lying in the escrow account, as applicable.
19.	Regulation 40	Transfer or transmission or transposition of securities	<p>The Board of directors may delegate the power of transfer of securities to a committee or to a compliance officer or to the share transfer agent.</p> <p>Such delegated authority shall attend to share transfer formalities once in a fortnight and shall report on the same to the Board of director.</p> <p>Transfer of securities</p> <ul style="list-style-type: none"> • On receipt of proper documentation, the listed entity shall register transfers of its securities in the name of the transferee(s) and issue certificates or receipts or advices, as applicable, of transfers; or issue any valid objection or intimation to the transferee or transferor, as the case may be, <i>within a period of 15 days from</i>

			<p><i>the date of such receipt of request for transfer.</i></p> <p>Transmission of securities</p> <ul style="list-style-type: none"> The listed entity shall ensure that transmission requests are processed for securities held in dematerialized mode and physical mode <i>within 7 days and 21 days respectively</i>, after receipt of the specified documents.
20.	Regulation 41	Other provisions relating to securities	<ul style="list-style-type: none"> The listed entity shall not exercise a lien on its fully paid shares or partly paid shares except in respect of moneys called or payable at a fixed time in respect of such shares. The listed entity shall not issue shares in any manner which may confer on any person, superior rights as to voting or dividend vis-à-vis the rights on equity shares that are already listed. The listed entity shall, issue or offer in the first instance all shares (including forfeited shares), securities, rights, privileges and benefits to subscribe pro-rata basis, to the equity shareholders of the listed entity, unless the shareholders in the general meeting decide otherwise. The listed entity shall not select any of its listed securities for redemption otherwise than on pro-rata basis or by lot.
21.	Regulation 42	Record Date or Date of closure of transfer books	<ul style="list-style-type: none"> Listed Company will intimate Stock Exchanges, <i>7 days in advance</i> about the record date for: <ul style="list-style-type: none"> (A) declaration of dividend (B) issue of right or bonus shares (C) issue of shares for conversion of debentures or any other convertible security. (D) corporate actions like mergers, demergers, splits and bonus shares. A listed entity shall recommend or declare all dividend and/or cash bonuses <i>at least 5 working days</i> (excluding the date of

			<p>intimation and the record date) <i>before the record date.</i></p> <ul style="list-style-type: none"> There shall be a gap <i>of at least 30 days</i> between two Record Dates.
22.	Regulation 43	Dividends	<ul style="list-style-type: none"> The listed entity shall declare and disclose the dividend on per share basis only. The listed entity shall not forfeit unclaimed dividends before the claim becomes barred by law and such forfeiture, if effected, shall be annulled in appropriate cases.
		Dividend Distribution Policy	<p>According to regulation 43A the top 500 listed entities based on market capitalization (calculated as on March 31 of every financial year) shall formulate a dividend distribution policy which shall be disclosed in their annual reports and on their websites.</p> <p>The dividend distribution policy shall include the following parameters:</p> <ul style="list-style-type: none"> the circumstances under which the shareholders of the listed entities may or may not expect dividend; the financial parameters that shall be considered while declaring dividend; internal and external factors that shall be considered for declaration of dividend; policy as to how the retained earnings shall be utilized; and parameters that shall be adopted with regard to various classes of shares: <p>However, if the listed entity proposes to declare dividend on the basis of parameters in addition to above mentioned clauses or proposes to change such additional parameters or the dividend distribution policy contained in any of the parameters, it shall disclose such changes along with the rationale for the same in its annual report and on its website.</p> <p>The listed entities excluding top 500 listed entities, may disclose their dividend distribution policies on a voluntary basis in their annual reports and on their websites.</p>

23.	Regulation 44	Voting by Shareholders	<ul style="list-style-type: none"> Listed Company to provide e-voting facility to all its shareholders, in respect of all shareholders' resolutions. Results of E-voting to be submitted <i>within 48 hours of conclusion of its General Meeting</i> in the format Specified by SEBI.
24.	Regulation 45	Change in name of the listed entity	<ul style="list-style-type: none"> The listed entity shall be allowed to change its name subject to compliance with the following conditions: <ul style="list-style-type: none"> a time period of <i>at least 1 year</i> has elapsed from the last name change; <i>at least fifty percent of the total revenue</i> in the preceding one year period has been accounted for by the new activity suggested by the new name; or the amount invested in the new activity/project is <i>atleast fifty percent of the assets</i> of the listed entity. On satisfaction of conditions, the listed entity shall file an application for name availability with Registrar of Companies. On receipt of confirmation regarding name availability from Registrar of Companies, the listed entity shall seek approval from Stock Exchange by submitting a certificate from chartered accountant stating compliance with conditions.
25.	Regulation 46	Website	<ul style="list-style-type: none"> The listed entity shall maintain a functional website containing the basic information about the listed entity. The listed entity shall disseminate the following information on its website: <ul style="list-style-type: none"> details of its business; terms and conditions of appointment of independent directors; composition of various committees of board of directors; code of conduct of board of directors and senior management personnel; details of establishment of vigil

			<p>mechanism/ Whistle Blower policy;</p> <ul style="list-style-type: none"> – criteria of making payments to non-executive directors , if the same has not been disclosed in annual report; – policy on dealing with related party transactions; – policy for determining ‘material’ subsidiaries; – details of familiarization programmes imparted to independent directors. – the email address for grievance redressal and other relevant details; – contact information of the designated officials of the listed entity who are responsible for assisting and handling investor grievances; – financial information including: <ul style="list-style-type: none"> (i) notice of meeting of the board of directors where financial results shall be discussed; (ii) Approved financial results. (iii) Complete copy of the annual report of the Company. – shareholding pattern; – details of agreements entered into with the media companies and/or their associates. <ul style="list-style-type: none"> • The listed entity shall ensure that the contents of the website are correct. • The listed entity shall update any change in the content of its website <i>within two working days from the date of such change in content.</i>
26.	Regulation 47	Advertisements in Newspapers	<ul style="list-style-type: none"> • The listed entity shall publish the following information in the newspaper: <ul style="list-style-type: none"> (a) Notice of meeting of the board of directors where financial results shall be discussed.

			<p>(b) Financial results along-with the modified opinion(s) or reservation(s), if any, expressed by the auditor.</p> <p>However, if the listed entity has submitted both standalone and consolidated financial results, the listed entity shall publish consolidated financial results along with Turnover, Profit before tax and Profit after tax, on a standalone basis, as a foot note; and a reference to the places, such as the website of listed entity and stock exchange(s), where the standalone results of the listed entity are available.</p> <p>(c) statements of deviation(s) or variation(s) on quarterly basis, after review by audit committee and its explanation in directors report in annual report;</p> <p>(d) Notices given to shareholders by advertisement published in at least one English language national daily newspaper circulating in the whole or substantially the whole of India and in one daily newspaper published in the language of the region, where the registered office of the listed entity is situated.</p>
27.	Regulation 48	Accounting Standards	The listed entity shall comply with all the applicable and notified Accounting Standards from time to time.

Compliance Calendar under SEBI (LODR) Regulations, 2015

- Quarterly;
- Half yearly;
- Annual; and
- Event based

Quarterly Compliances

Regulation	Particulars	Period	Due date
13(3)	Statement Grievance Redressal Mechanism	Apr-Jun, Jul-Sep, Oct-Dec, Jan-Mar	21 st Jul, 21 st Oct, 21 st Jan 21 st Apr
31(1)(b)	Shareholding Pattern	-do-	-do-
32(1)	Statement of deviation or variation	-do-	-do-
27(2)(a)	Corporate Governance Report	Apr-Jun, Jul-Sep, Oct-Dec, Jan-Mar	15 th Jul, 15 th Oct, 15 th Jan 15 th Apr
33(3)(a)	Financial Results	Apr-Jun, Jul-Sep, Oct-Dec, Jan-Mar	14 th Aug 14 th Nov 14 th Feb 14 th May

Half yearly Compliances

Regulation	Particulars	Period	Due date
7(3)	Compliance Certificate to the exchange	Apr-Sep,	31st Oct,
		Oct-Mar	30th Apr
40(10)	Compliance Certificate w.r.t Transfer or transmission or transposition of securities within 30 Days	-do-	-do-

Annual Compliances

Regulation	Particulars	Period	Due date
14	Listing fees	Apr-Mar	30th Apr
33(3)(d)	Financial Results	Apr-Mar	30th May
34(1)	Annual Report	Apr-Mar	Within 21 working days from AGM

Event Based Compliances

Regulation	Particulars	Due date
7(5)	Intimation of appointment of Share Transfer Agent	Within 7 days of Agreement with RTA

28(1)	In-principle approval	Prior to issuance of Security
29(1)(a) read along with proviso to 29 (2)	Prior intimations of Board Meeting for financial Result viz. Quarterly, half yearly or annual	At least 5 clear days in advance
29(1)(b), (c),(d), (e) & (f) read along with 29 (2)	Prior intimations of Board Meeting for Buy-back, Voluntary delisting , Fund raising by way of FPO, Rights Issue, ADR, GDR, QIP, FCCB, Preferential issue, debt issue or any other method, Declaration/ recommendation of dividend, issue of convertible securities carrying a right to subscribe to equity shares or the passing over of dividend, proposal for declaration of Bonus securities etc	At least 2 days in advance
29(3)	Prior intimations of Board Meeting for alteration in nature of Securities	At least 11 clear working days in Advance
30(6)	Disclosure of Price Sensitive Information	Not later than twenty four hours as per Part A of Schedule III
31(1)(a)	Shareholding Pattern prior to listing of Securities	One day prior to listing of Securities
31(1)(c)	Shareholding Pattern in case of capital Restructuring	Within 10 days of any change in capital structure exceeding 2%
37(2)	Draft Scheme of Arrangement	Prior approval before filing with Court
42(2)	Record date or Date of closure of transfer books	At least 7 clear working days in Advance
42(3)	Record date for declaring dividend and / or cash bonus	At least 5 clear working days in Advance
44(3)	Voting results by Shareholders	Within 48 Hours
45(3)	Change in name of listed Entity	Prior approval

Consequences of Non-Compliance

To ensure effective enforcement of compliances by listed entity, SEBI has decided in consultation with recognized stock exchanges to freeze the holdings of their promoters and promoter group entities in the manner specified below:

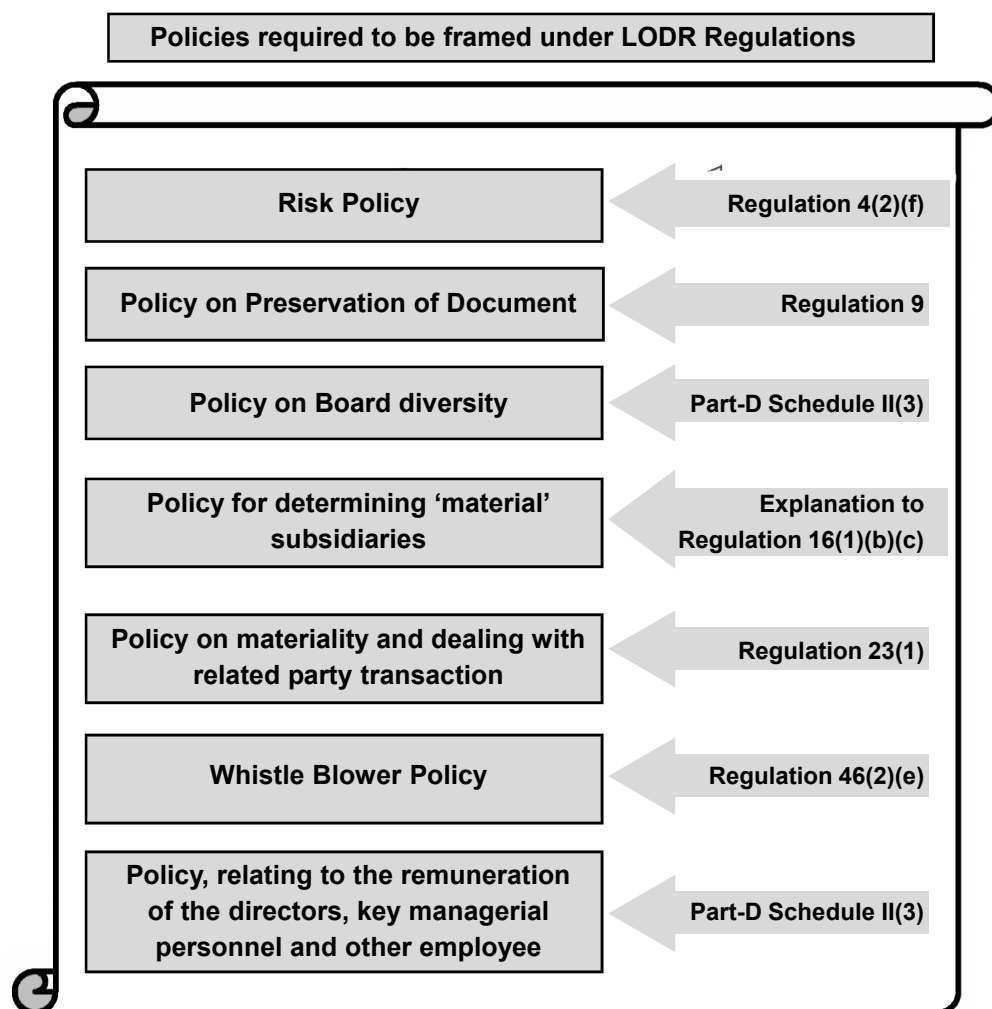
1. Where a non-compliant listed entity fails to pay fine levied as per the notice issued by the concerned recognized stock exchange, the concerned recognized stock exchange shall, upon expiry of the period indicated in the notice issued by it, freeze holdings in other securities in the demat accounts of promoter and promoter group to the extent of liability which shall be calculated on a quarterly basis.
2. In case of non-compliance for two consecutive periods, and failure to comply with the notice issued by the concerned recognized stock exchange, as per the current practice, the concerned recognized stock exchange shall forthwith intimate the depositories to freeze the entire shareholding of the promoter and promoter group in such listed entity. In addition to the freeze of shares in the non-compliant listed entity,

the holdings in the demat accounts of promoter and promoter group in other securities shall also be frozen to the extent of liability which shall be calculated on a quarterly basis.

3. While freezing the holdings, the recognized stock exchange shall have discretion in determining which of the securities and holdings of which promoter or promoter group entity are to be frozen.

The depositories, shall furnish to the exchange upon receipt of request, all such information pertaining to holdings in the demat accounts of promoter and promoter group of such listed entities.

POLICIES UNDER LODR REGULATION



CORPORATE GOVERNANCE

Corporate governance denotes the process, structure and relationship through which the Board of Directors oversees what the management does. It is also about being answerable to different stakeholders.

CII constituted a Committee to recommend a Code of Corporate Governance to be observed by corporates in their functioning. The Committee further recommended a Code popularly known as “Desirable Corporate Governance Code” which defined Corporate Governance as follows:

“Corporate governance deals with laws, procedures, practices and implicit rules that determine a company’s ability to take informed managerial decisions vis-à-vis its claimants – in particular, its shareholders, creditors, customers, the State and employees. There is a global consensus about the objective of ‘good’ corporate governance: maximising long-term shareholder value.”

The Kumar Mangalam Birla Committee Constituted by SEBI has observed that:

“Strong corporate governance is indispensable to resilient and vibrant capital markets and is an important instrument of investor protection. It is the blood that fills the veins of transparent corporate disclosure and high-quality accounting practices. It is the muscle that moves a viable and accessible financial reporting structure.”

N.R. Narayana Murthy Committee on Corporate Governance constituted by SEBI has observed that:

“Corporate Governance is the acceptance by management of the inalienable rights of shareholders as the true owners of the corporation and of their own role as trustees on behalf of the shareholders. It is about commitment to values, about ethical business conduct and about making a distinction between personal and corporate funds in the management of a company.”

The Institute of Company Secretaries of India has also defined the term Corporate Governance as under:

Good Governance in capital market has always been high on the agenda of SEBI. Corporate Governance is looked upon as a distinctive brand and benchmark in the profile of Corporate Excellence. This is evident from the continuous updation of guidelines, rules and regulations by SEBI for ensuring transparency and accountability. In the process, SEBI had constituted a Committee on Corporate Governance under the Chairmanship of Shri Kumar Mangalam Birla. The Committee in its report observed that “the strong Corporate Governance is indispensable to resilient and vibrant capital markets and is an important instrument of investor protection. It is the blood that fills the veins of transparent corporate disclosure and high quality accounting practices. It is the muscle that moves a viable and accessible financial reporting structure.”

Based on the recommendations of the Committee, the SEBI had specified principles of Corporate Governance and introduced a new clause 49 in the Listing agreement of the Stock Exchanges in the year 2000. These principles of Corporate Governance were made applicable in a phased manner and all the listed companies with the paid up capital of Rs 3 crores and above or net worth of Rs 25 crores or more at any time in the history of the company, were covered as of March 31, 2003.

SEBI, as part of its endeavour to improve the standards of corporate governance in line with the needs of a dynamic market, constituted another Committee on Corporate Governance under the Chairmanship of Shri N. R. Narayana Murthy to review the performance of Corporate Governance and to determine the role of companies in responding to rumour and other price sensitive information circulating in the market in order to enhance the transparency and integrity of the market. The Committee in its Report observed that “the effectiveness of a system of Corporate Governance cannot be legislated by law, nor can any system of Corporate Governance be static. In a dynamic environment, system of Corporate Governance need to be continually evolved.”

With a view to promote and raise the standards of Corporate Governance, SEBI on the basis of recommendations of the Committee and public comments received on the report and in exercise of powers conferred by Section 11(1) of the SEBI Act, 1992 read with section 10 of the Securities Contracts (Regulation) Act 1956, revised the existing clause 49 of the Listing agreement vide its circular SEBI/MRD/SE/31/2003/26/08 dated August 26, 2003.

SEBI vide circular number SEBI/CFD/ DIL/CG/1/2004/12/10 dated October 29, 2004 again revised the existing Clause 49 of the Listing Agreement directing all the Stock Exchanges to amend the Listing Agreement by replacing the existing Clause 49 of the Listing Agreement. As per the Circular, the provisions of the Clause 49 were to be implemented as per the schedule of implementation given below:

- (a) For entities seeking listing for the first time, at the time of seeking in-principle approval for such listing.
- (b) For existing listed entities which were required to comply with Clause 49 which is being revised i.e. those having a paid up share capital of Rs. 3 crores and above or net worth of Rs. 25 crores or more at any time in the history of the company, by April 1, 2005.

However, noticing that large number of companies were not in the state of preparedness to be fully compliant with the requirements of revised Clause 49 of the listing agreement, SEBI allowed more time to corporates to conform to Clause 49 of the listing agreement and extended the date for ensuring compliance with the Clause 49 of the listing agreement to December 31, 2005.

The Companies Act, 2013 was enacted on August 30, 2013 which provides for a major overhaul in the Corporate Governance norms for all companies. The rules pertaining to Corporate Governance were notified on March 27, 2014. The requirements under the Companies Act, 2013 and the rules notified thereunder would be applicable for every company or a class of companies (both listed and unlisted) as may be provided therein. SEBI reviewed the provisions of the Listing Agreement in this regard with the objectives to align with the provisions of the Companies Act, 2013, adopt best practices on corporate governance and to make the corporate governance framework more effective. SEBI vide its circular dated April 17, 2014, revised new clause 49 in alignment with Companies Act, 2013.

Further as a good governance initiative and with a view to consolidate and streamline the provisions of listing agreement of the capital market and to align the provisions relating to listed entities with the Companies Act, 2013 SEBI notified the Listing Regulations replacing the earlier listing agreement.

CORPORATE GOVERNANCE UNDER SEBI (LODR), 2015

S. No.	Regulation No.	Subject	Particulars
1.	Regulation 16(1)(b)	Independent Director	<p>Independent Director” means a non-executive director, other than a nominee director of the listed entity –</p> <ul style="list-style-type: none"> – who, in the opinion of the board of directors, is a person of integrity and possesses relevant expertise and experience; – who is or was not a promoter of the listed entity or its holding, subsidiary or associate company; – who is not related to promoters or directors in the listed entity, its holding, subsidiary or associate company; – who, apart from receiving director’s remuneration, has or had no material pecuniary relationship with the listed entity, its holding, subsidiary or associate company, or their promoters, or directors, during the two immediately preceding financial years or during the current financial year; – none of whose relatives has or had pecuniary relationship or transaction with the listed entity, its holding, subsidiary or associate company, or their promoters, or directors, amounting to two per cent or more of its gross turnover or total income or Rs. 50 lakh or such higher amount as may be prescribed from time to time, whichever is lower, during the two immediately preceding financial years or during the current financial year; – who, neither himself, nor whose relative(s)

			<p>holds or has held the position of a key managerial personnel or is or has been an employee of the listed entity or its holding, subsidiary or associate company in any of the three financial years immediately preceding the financial year in which he is proposed to be appointed;</p> <ul style="list-style-type: none"> – who, neither himself, nor whose relative(s) is or has been an employee or proprietor or a partner, in any of the three financial years immediately preceding the financial year in which he is proposed to be appointed,
2.	Regulation 17(1)	Composition of Board of Directors	<p>The Composition of Board of directors of the listed entity shall be as follows:</p> <p>Executive/Non Executive:</p> <ul style="list-style-type: none"> – Board of Directors shall have an optimum combination of executive and non-executive directors:- <ul style="list-style-type: none"> • One Women Director • At least 50% of Board of Directors shall comprise of Non-Executive Director. <p>Independent Director:</p> <ul style="list-style-type: none"> – If Chairman of the Board is Non-Executive director <ul style="list-style-type: none"> • at least (1/3) one-third of the board of directors shall comprise of independent directors. – where the listed entity does not have a regular non-executive chairperson <ul style="list-style-type: none"> • at least (1/2) half of the board of directors shall comprise of independent directors – where the regular non-executive chairperson is a promoter of the listed entity; or is related to any promoter; or is related to person occupying management positions at the level of board of director; or at one level below the board of directors; <ul style="list-style-type: none"> • at least (1/2) half of the board of directors of the listed entity shall consist of independent directors.
3.	Regulation 17(2)	Frequency of Meeting	<ul style="list-style-type: none"> – At least 4 Board meeting

			<ul style="list-style-type: none"> – Maximum Gap Between two meetings 120 days
4.	Regulation 17(3)	Review of Compliance report	<ul style="list-style-type: none"> – The board of directors shall periodically review compliance reports pertaining to all laws applicable to the listed entity. – The board of directors shall periodically review steps taken by the listed entity to rectify instances of non-compliances.
5.	Regulation 17(4) & (5)	Duties of Board of Directors	<ul style="list-style-type: none"> – Plans for Ordinary succession of appointment: The board of directors of the listed entity shall satisfy itself that plans are in place for orderly succession for appointment to the board of directors and senior management. – Code of Conduct: The board of directors shall lay down a Code of Conduct for all members of board of directors and senior management of the listed entity. – Duties of Independent Director: The code of conduct shall suitably incorporate the duties of independent directors as laid down in the Companies Act, 2013.
6.	Regulation 17(6)	Fees or Compensation	<ul style="list-style-type: none"> – The board of directors shall recommend all fees or compensation, if any, paid to non-executive directors, including independent directors and shall require approval of Shareholders in General Meetings. – The requirement of obtaining approval of shareholders in General Meeting shall not apply to payment of sitting fees to Non-Executive Directors, if made within the limits prescribed under Companies Act, 2013. <i>Approval of shareholders mentioned above, shall specify the limits for the maximum number of stock options that may be granted to non-executive directors, in any financial year and in aggregate.</i> – Independent Director shall not entitle to any Stock Option.
7.	Regulation 17(8)	Compliance Certificate	The Chief Executive Officer and the Chief Financial Officer shall provide the compliance certificate to the board of directors.

8.	Regulation 17(10)	Performance evaluation	The performance evaluation of independent directors shall be done by the entire board of directors. However, in the above evaluation the directors who are subject to evaluation shall not participate.
9.	Regulation 18	Audit Committee	<ul style="list-style-type: none"> • Every Listed Entity shall constitute a Qualified and independent audit committee in accordance with the terms subject to the followings:- <ul style="list-style-type: none"> – The audit committee shall have minimum three directors as members and – 2/3 (Two-thirds) of the members of committee shall be independent directors. – All members of Committee shall be financially literate and at least one member has expertise in accounting or related financial management. – The chairperson of the audit committee shall be an independent director and he shall be present at AGM to answer shareholder queries. – The Company Secretary shall act as the secretary to the audit committee. • The listed entity shall conduct the meetings of the audit committee in the following manner: <ul style="list-style-type: none"> – Four Meetings in a year – Maximum gap between two meetings 120 days – Quorum shall be 2 members or 1/3rd of the members of the audit committee, whichever is greater, with at least 2 independent directors. – The audit committee shall have powers to investigate any activity within its terms of reference, seek information from any employee, obtain outside legal or other professional advice and secure attendance of outsiders with relevant expertise, if it considers necessary. <p>Note: - The Role of the audit committee and the INFORMATION TO BE REVIEWD by the audit</p>

			<i>committee shall be as specified in Part C of Schedule II.</i>
10.	Regulation 19	Nomination and remuneration committee	<ul style="list-style-type: none"> The Board of Directors shall constitute the nomination and remuneration committee as follows: <ul style="list-style-type: none"> The committee shall comprise of at least three directors. All the directors of the committee shall be Non-Executive directors and At least 50% of the directors shall be Independent directors. The Chairperson of the nomination committee shall be independent director. However, where chairperson of listed entity is executive or non-executive, may appoint as a member and shall not chair such committee. The chairperson of such committee may present at the AGM, to answer the shareholder's queries.
11.	Regulation 20	Stakeholder Relationship Committee	<p>Purpose of constitution :- To look into the mechanism of redressal of grievances of :-</p> <ul style="list-style-type: none"> shareholders, debenture holders and other security holders <ul style="list-style-type: none"> The chairperson of such committee shall be a Non-Executive Director.
12.	Regulation 21	Risk Management Committee	<ul style="list-style-type: none"> The board of directors shall constitute Risk Management Committee, shall be define the role and responsibility of the Risk Management Committee, and may delegate monitoring and reviewing of the risk management plan to the committee and such other functions as it may deem fit. The majority of members of such Committee shall consist of members of the board of directors. The Chairperson of such committee shall be a member of the board of directors and senior executives of the listed entity may be members of the committee.

13.	Regulation 24	Subsidiary Companies	<p>Corporate governance requirements with respect to subsidiary of listed entity</p> <ul style="list-style-type: none"> – At least one independent director of the listed entity shall be a director on the board of directors of an unlisted material subsidiary, incorporated in India. – The audit committee of the listed entity shall also review the financial statements, in particular, the investments made by the unlisted subsidiary. – The minutes of the meetings of the board of directors of the unlisted subsidiary shall be placed at the meeting of the board of directors of the listed entity. – The management of the unlisted subsidiary shall periodically bring to the notice of the board of directors of the listed entity, a statement of all significant transactions and arrangements entered into by the unlisted subsidiary. – A listed entity shall not dispose of shares in its material subsidiary resulting in reduction of its shareholding (either on its own or together with other subsidiaries) to less than fifty percent or cease the exercise of control over the subsidiary without passing a special resolution in its General Meeting except in cases where such divestment is made under a scheme of arrangement duly approved by a Court/ Tribunal. – Selling, disposing and leasing of assets amounting to more than twenty percent of the assets of the material subsidiary on an aggregate basis during a financial year shall require prior approval of shareholders by way of special resolution, unless the sale/disposal/ lease is made under a scheme of arrangement duly approved by a Court/Tribunal. – Where a listed entity has a listed subsidiary, which is itself a holding company, the provisions of this regulation shall apply to the listed subsidiary in so far as its subsidiaries are concerned.
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14.	Regulation 25	<p>Obligations with respect to Independent directors:-</p> <ul style="list-style-type: none"> – Limit of Directorship as Independent Director – Tenure of Independent Director – Meeting of Independent Director – Agenda for the Meeting of Independent Director – Liability of Independent Director 	<p>Obligations with respect to Independent directors:-</p> <ul style="list-style-type: none"> • A person shall serve as an independent director not more than seven listed entities. If such person is whole time director in any entities then he shall be serving as independent director not more than three listed entities. • Maximum tenure of independent director shall be up to five consecutive years on the Board of director of a company. He shall be eligible for reappointment on passing of a special resolution by the company and disclosure of such appointment in the Board's report. • The independent directors of the listed entity shall hold at least one meeting in a year. Non-Independent Director and Members of the Management will not present in such Meeting. All the Independent Directors shall strives to present in such Meeting. • The Independent director in the meeting shall :- <ul style="list-style-type: none"> – Review the performance of non-independent directors and the board of directors as a whole – Review the performance of the chairperson of the listed entity.(Taking into account the views of executive directors and non-executive directors) – Assess the quality, quantity and timeliness of flow of information between the management of the listed entity and the board of directors that is necessary for the board of directors to effectively and reasonably perform their duties • An independent director shall be held liable, ONLY in respect of such acts of omission or commission by the listed entity which had occurred:- <ul style="list-style-type: none"> – with his knowledge and – attributable through processes of board of directors, and – with his consent or connivance or
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		<ul style="list-style-type: none"> – Intermittent vacancy of an Independent Director – Duties of the Company towards Independent Director 	<ul style="list-style-type: none"> – Where he had not acted diligently with respect to the provisions contained in these regulations. • Any Intermittent Vacancy of an Independent director shall be filled-up by the Board of Directors at the earliest but not later than:- <ul style="list-style-type: none"> – Immediate Next Board Meeting OR – 3 (Three) Months from the date of such vacancy, whichever is Later • The listed entity shall familiarize the independent directors through various programmes about the listed entity, including the following:- <ul style="list-style-type: none"> – Nature of the industry in which the listed entity operates; – Business model of the listed entity; – Roles, rights, responsibilities of independent directors; and – Any other relevant information
15.	Regulation 26	Obligations with respect to employees including senior management key managerial person, directors and promoters	<p>For the purpose of considering the limit of companies Private Company, Foreign Company and Section 8 of Companies Act, 2013 company are excluded.</p> <p>A Director shall not be :-</p> <ul style="list-style-type: none"> – Member in more than 10 committees – Chairman in more than 5 committees <p>For reckoning the limit, ONLY Audit committee and Stakeholder's relationship Committee are considered.</p> <p>No employee including key managerial personnel or director or promoter of a listed entity shall enter into any agreement for himself or on behalf of any other person, with any shareholder or any other third party with regard to compensation or profit sharing in connection with dealings in the securities of such listed entity, unless prior approval for the same has been obtained from the Board of Directors as well as public shareholders by way of an ordinary resolution.</p> <p>However, such agreement, if any, whether subsisting or expired, entered during the</p>

			<p>preceding three years from the date of coming into force of this sub-regulation, shall be disclosed to the stock exchanges for public dissemination.</p> <p>Further that subsisting agreement, if any, as on the date of coming into force of this sub-regulation shall be placed for approval before the Board of Directors in the forthcoming Board meeting.</p> <p>If the Board of Directors approve such agreement, the same shall be placed before the public shareholders for approval by way of an ordinary resolution in the forthcoming general meeting.</p> <p>All interested persons involved in the transaction covered under the agreement shall abstain from voting in the general meeting.</p>
16.	Regulation 27	Quarterly Compliance Report on Corporate Governance	<ul style="list-style-type: none"> • The listed entity shall submit a quarterly compliance report on corporate governance in the format as specified by SEBI from time to time to the recognized stock exchange(s) <i>within fifteen days from close of the quarter.</i> • Details of all material transactions with related parties shall be disclosed. • Report shall be sign either by Compliance officer or by Chief Executive officer.

Corporate Governance - Listing Regulations vis-a-vis Companies Act 2013

S.No.	Particulars	Listing Regulations	Companies Act 2013
1.	Size of the Board	Regulation 17(1)(a)	Section 149 (1)
		The board of directors shall have an optimum combination of executive and non-executive directors.	It stipulates the minimum number of director as three in case of public company, two in case of private company and one in case of One Person Company. The maximum number of directors stipulated is 15.
2.	Board Composition	Regulation 17(1) <ul style="list-style-type: none"> • At least 50% of the board of directors shall comprise of non-executive directors. • If the chairperson of the board of 	Section 149(4) provides that every public listed Company shall have atleast one third of total number of directors as independent directors and Central Government may further prescribe

		<p>directors is a non-executive director, at least 1/3rd of the board of directors shall comprise of independent directors.</p> <ul style="list-style-type: none"> • If the chairperson of the board of directors is not a non-executive director, at least 50% of the board of directors shall comprise of independent directors. • If the regular non-executive chairperson is a promoter of the listed entity or is related to any promoter or person occupying management positions at the level of board of director or at one level below the board of directors, at least 50% of the board of directors of the listed entity shall consist of independent directors. 	<p>minimum number of independent directors in any class or classes of company.</p> <p>Rule 4 of the Companies (Appointment and Qualification of Directors) Rules, 2014 prescribes that the following class or classes of companies shall have at least two independent directors:</p> <ul style="list-style-type: none"> • Public Companies having paid-up share capital of 10 crore rupees or more; or • Public Companies having turnover of 100 crore rupees or more; or • Public Companies which have, in aggregate, outstanding loans, debentures and deposits, exceeding 50 crore rupees.
3.	Appointment of Woman Director	<p>Regulation 17(1)(a)</p> <p>The Board of Directors of the Listed Entity shall have at least one woman director.</p>	<p>Section 149(1) and Companies (Appointment and Qualification of Directors) Rules, 2014</p> <p>Rule (3) read with Section 149(1) provides that</p> <p>(i) every listed company;</p> <p>(ii) every other public company having -</p> <p>(a) paid-up share capital of Rs.100 crores or more; or</p> <p>(b) Turnover of Rs.300 crore or more shall appoint at least one woman director.</p> <p>A company shall comply with provisions within a period of six months from the date of its incorporation.</p> <p>Any intermittent vacancy of a woman director shall be filled up by the Board of directors at the earliest but not later than immediate next Board meeting or three months from the date of such vacancy whichever is later.</p>
4.	Maximum No. of directorship of IDs.	<p>Regulation 25(1)</p> <p>A person shall not serve as an independent director in more than seven listed Entities.</p> <p>Any person who is serving as a</p>	<p>Section 165</p> <p>A person shall not hold office as a director, including any alternate directorship in more than 20 companies at the same time. The max no. of public</p>

		whole time director in any listed Entity shall serve as an independent director in not more than three listed Entities.	companies in which a person can be appointed as a director shall not exceed 10.
5.	Maximum tenure of IDs	Regulation 25(2) It shall be in accordance with the Companies Act 2013 and rules made thereunder, in this regard, from time to time.	Section 149(10) & (11) Subject to the provisions of Section 152(2), an independent director shall hold office for a term up to five consecutive years on the Board of directors of a company, but shall be eligible for reappointment on passing of a special resolution by the company and disclosure of such appointment in the Board's report. No independent director shall hold office for more than two consecutive terms, but such independent director shall be eligible for appointment after the expiration of three years of ceasing to become an independent director.
6.	Performance evaluation of IDs	(a) The Nomination Committee shall lay down the evaluation criteria for performance evaluation of independent directors. (b) The Listed Entities shall disclose the criteria for performance evaluation, as laid down by the Nomination Committee, in its Annual Report. (c) The performance evaluation of independent directors shall be done by the entire Board of Directors. (d) On the basis of the report of performance evaluation, it shall be determined whether to extend or continue the term of appointment of the independent director.	Section 178(2) read with Schedule IV The Nomination and Remuneration Committee shall identify persons who are qualified to become directors and who may be appointed in senior management in accordance with the criteria laid down, recommend to the Board of directors their appointment and removal and shall carry out evaluation of every director's performance. The performance evaluation of independent directors shall be done by the entire Board of Directors, excluding the director being evaluated. On the basis of the report of performance evaluation, it shall be determined whether to extend or continue the term of appointment of the Independent Director.
7.	Separate meeting of IDs	Regulation 25(3) The IDs of shall hold at least one meeting in a year, without the attendance of non-independent directors and members of management. All the independent directors of the Listed Entity shall strive to be present at such meeting.	Section 149 read with Schedule IV IDs of the company shall hold at least one meeting in a year, without the attendance of non-independent directors and members of management. All the independent directors of the company shall strive to be present at such meeting.

8.	Familiarisation Programme for Independent Director	Regulation 25(7) The Listed Entity shall familiarise the independent directors with the Listed Entity, their roles, rights, responsibilities in the Listed Entity, nature of the industry in which the Listed Entity operates, business model of the Listed Entity, etc. The details of such familiarisation programme shall be disclosed on Listed Entity website and a web link thereto shall also be given in the Annual Report.	Schedule IV specifies that the Independent Directors shall undertake appropriate induction and regularly update and refresh their skills, knowledge and familiarity with the company.
9.	Prohibited Stockoptions for IDs	Regulation 17(6)(d) IDs shall not be entitled to any stock options.	Section 197(7) IDs shall not be entitled to any stock option.
10.	Filing of Casual Vacancy of IDs	Regulation 25(6) An independent director who resigns or is removed from the Board of directors of the Listed Entity shall be replaced by a new independent director at the earliest but not later than the immediate next Board meeting or three months from the date of such vacancy, whichever is later. However, where the Listed Entity fulfils the requirement of independent directors in its Board of directors even without filling the vacancy created by such resignation or removal, as the case may be, the requirement of replacement by a new independent director shall not apply.	Schedule IV, Section VI An independent director who resigns or is removed from the Board of director of the company shall be replaced by a new independent director within a period of not more than one hundred and eighty days from the date of such resignation or removal, as the case may be. Where the company fulfils the requirement of independent directors in its Board of directors even without filling the vacancy created by such resignation or removal, as the case may be, the requirement of replacement by a new Independent Director shall not apply.
11.	Succession planning	Regulation 17(4) The Board of directors of the Listed Entity shall satisfy itself that plans are in place for orderly succession for appointments to the Board of directors and to senior management.	There is no such provision.
12.	Code of Conduct of Board of Directors & Senior Management	Regulation 17(5) The Board of directors shall lay down a code of conduct for all Board members and seniors management of the Listed Entity. The code of conduct shall be posted on the website of the Listed Entity. All Board members and senior	Section 149 (8) provides that the company and the independent directors shall abide by the provisions specified in Schedule IV.

		<p>management personnel shall affirm compliance with the code on an annual basis. The Annual Report of the Listed Entity shall contain a declaration to this effect signed by the CEO.</p> <p>The Code of Conduct shall suitably incorporate the duties of Independent Directors as laid down in the Companies Act, 2013.</p>	
13.	Liability of IDs	<p>Regulation 25 (5) An independent director shall be held liable, only in respect of such acts of omission or commission by a Listed Entity which had occurred with his knowledge, attributable through Board of director processes, and with his consent or connivance or where he had not acted diligently with respect of the provisions contained in the Listing Agreement.</p>	<p>Section 149(12) An independent director; a need not being promoter or KMP, shall be held liable, only in respect of such acts of omission or commission by a company which had occurred with his knowledge, attributable through Board of directors processes, and with his consent or connivance or where he had not acted diligently.</p>
14.	Vigil mechanism	<p>Regulation 22 The Listed Entity shall establish a vigil mechanism for directors and employees to report concerns about unethical behaviour, actual or suspected fraud or violation of the Listed Entity code of conduct or ethics policy. This mechanism should also provide for adequate safeguards against victimization of director(s)/ employee(s) who avail of the mechanism and also provide for direct access to the chairperson of the Audit Committee in exceptional cases. The details of establishment of such mechanism shall be disclosed by the Listed Entity on its website and in the Board's report.</p>	<p>Section 177(9) read with Rule 7 of Companies (Meeting of Board and its Power) Rules, 2014 Every listed company or such class or classes of companies to establish a Vigil mechanism for directors and employees to report genuine concern. The details of establishment of Vigil mechanism shall be disclosed by the company in the website, if any, and in the Board's Report. Rule 7 of Companies (Meeting of Board and its Power) Rules, 2014 states that the companies which are required to constitute an audit committee shall oversee the vigil mechanism through the committee and if any of the members of the committee have a conflict of interest in a given case, they should rescue themselves and the others on the committee would deal with matter on hand. The Vigil Mechanism shall provide adequate safeguards against victimization of employees and directors who avail of the Vigil mechanism and also provide for direct</p>

			access to the chairperson of the Audit committee or the director nominated to play the role of audit committee, as the case may be, in exceptional cases.
15.	Qualification of IDs	The qualifications of IDs are not specified in the Listed Regulation.	<p>Rule 5 of Companies (Appointment and Qualification of Directors) Rules, 2014</p> <p>An independent director shall possess appropriate skills, experience and knowledge in one or more fields of finance, law, management, sales, marketing, administration, research, corporate governance, technical operations or other disciplines related to the company's business.</p>
16.	Constitution of Audit Committee	<p>Regulation 18</p> <p>A listed Entity shall set up a qualified and independent audit committee shall be set up, giving the terms of reference subject to the following:</p> <ol style="list-style-type: none"> 1. The audit committee shall have minimum three directors as members. Two-thirds of the members of audit committee shall be independent directors. 2. All members of audit committee shall be financially literate and at least one member shall have accounting or related financial management expertise. 3. The chairperson of the Audit Committee shall be an Independent Director. 	<p>Section 177 read with Rule 6 of Companies (Meeting of Board and Its Powers) Rules, 2014 states that the Board of directors of every listed company and such class of companies as prescribed under Rule 6, shall constitute an Audit Committee. The Audit Committee shall consist of a minimum three directors with independent directors forming a majority provided that majority of members of Audit Committee including its chairperson shall be person with ability to read and understand the financial statement.</p>
17.	Constitution of Nomination & Remuneration Committee	<p>Regulation 19</p> <p>The Listed Entity through its Board of directors shall constitute the nomination and remuneration committee which shall comprise at least 3 directors, all of whom shall be non-executive directors and at least ½ shall be independent.</p> <p>A. Chairperson of the committee shall be an Independent Director. However, the chairperson of the Listed Entity (whether executive</p>	<p>Section 178 and Rule 6 of Companies (Meetings of Board and its Powers) Rules, 2014</p> <p>The Board of directors of every listed companies and such class or classes of companies as prescribed under Rule 6, shall constitute a Nomination and Remuneration Committee of the Board of directors.</p> <p>The above mentioned companies shall constitute the Nomination and Remuneration Committee consisting of 3 or more non- executive directors out</p>

		<p>or non-executive) may be appointed as a member of the Nomination and remuneration Committee but shall not chair such Committee.</p> <p>B. The role of the committee shall, inter-alia, include the following:</p> <ol style="list-style-type: none"> 1. Formulation of the criteria for determining qualifications, positive attributes and independence of a director and recommend to the Board of directors a policy, relating to the remuneration of the directors, KMP and other employees; 2. Formulation of criteria for evaluation of IDs and the Board of directors; 3. Devising a policy on Board of directors diversity; 4. Identifying persons who are qualified to become directors and who may be appointed in senior management in accordance with the criteria laid down, and recommend to the Board of directors their appointment and removal. The Listed Entity shall disclose the remuneration policy and the evaluation criteria in its Annual Report. <p>C. The Chairperson of the nomination and remuneration committee could be present at the AGM, to answer the shareholders' queries. However, it would be up to the Chairperson to decide who should answer the queries.</p>	<p>of which not less than one half shall be IDs.</p> <p>The chairperson of the company (whether executive or non-executive) may be appointed as a member of the Nomination and Remuneration Committee but shall not chair such Committee. The Nomination and Remuneration Committee shall -</p> <ul style="list-style-type: none"> • Identify persons who are qualified to become directors and who may be appointed in senior management in accordance with the criteria laid down, recommend to the Board of directors their appointment and removal, carry out evaluation of every director's performance. • Formulate the criteria for determining qualifications, positive attributes and independence of a director and Recommend to the Board of directors a policy, relating to the remuneration for the directors, key managerial personnel and other employees. <p>The Nomination and Remuneration Committee shall while formulating the policy ensure that—</p> <ol style="list-style-type: none"> (a) the level and composition of remuneration is reasonable and sufficient to attract, retain and motivate directors of the quality required to run the company successfully; (b) relationship of remuneration to performance is clear and meets appropriate performance benchmarks; and (c) remuneration to directors, KMPs and senior management involves a balance between fixed and incentive pay reflecting short and long-term performance objectives appropriate to the working of the company and its goals: <p>The policy shall be disclosed in the Board's report.</p>
18.	Risk management	<p>Regulation 21</p> <p>The top 100 Listed entities,</p>	<p>Section 134(3)(n)</p> <p>The Board's report as prescribed under</p>

		<p>determined on the basis of market capitalisation shall lay down procedures to inform Board of directors members about the risk assessment and minimization procedures. The Board of directors shall be responsible for framing, implementing and monitoring the risk management plan for the Listed Entity.</p> <p>The Listed Entity through its Board of director shall constitute a Risk Management Committee. The Board of directors shall define the roles and responsibilities of the Risk Management Committee and may delegate monitoring and reviewing of the risk management plan to the committee and such other functions as it may deem fit.</p> <p>The majority of Committee shall consist of members of the Board of Directors. Senior executives of the Listed Entity may be members of the said Committee but the Chairperson of the Committee shall be a member of the Board of Directors.</p>	<p>Section 134(3) required to include in the Board's Report, a statement indicating development and implementation of a risk management policy for the company including identification therein of elements of risk, if any, this in the opinion of the Board of directors may threaten the existence of the company.</p>
19.	Related Party	<p>Clause 2(zb) For the purpose of Listing Regulation, an entity shall be considered as related to the Listed Entity if:</p> <ol style="list-style-type: none"> i. Such entity is a related party under Section 2(76) of the Companies Act, 2013; or (ii) Such entity is a related party under the applicable accounting standards. 	<p>Section 2(76) “Related party”, with reference to a company, means—</p> <ol style="list-style-type: none"> (i) a director or his relative (ii) a KMP or his relative; (iii) a firm, in which a director, manager or his relative is a partner; (iv) a private company in which a director or manager or his relative is a member or director; (v) a public company in which a director or manager is a director and holds along with his relatives, more than 2% of its paid-up share capital; (vi) any body corporate whose Board of Directors, managing director or manager is accustomed to act in accordance with the advice,

			<p>directions or instructions of a director or manager;</p> <p>(vii) any person on whose advice, directions or instructions a director or manager is accustomed to act;</p> <p>(viii) any company which is</p> <p>(A) a holding, subsidiary or an associate company of such company; or</p> <p>(B) a subsidiary of a holding company to which it is also a subsidiary.</p> <p>(viii) such other person as may be prescribed. Rule 3 of the Companies (Specification of Definitions Details) Rules, 2014 provides that a director or key managerial personnel of the holding company or his relative with reference to a company shall be deemed to be a related party.</p>
20.	Disclosure of RPTs	<p>Regulation 27(2)(a)</p> <p>Details of all material transactions with related parties shall be disclosed quarterly along with the compliance report on corporate governance. The Listed Entity shall disclose the policy on dealing with RPTs on its website and a web link thereto shall be provided in the Annual Report.</p>	<p>Section 134(3)(h) mandates that Board's Report shall contain particulars of contracts or arrangements with related party as referred in section 188 of the Companies Act, 2013.</p>
21.	Disclosure of different Accounting Standard	<p>Regulation 34(3)</p> <p>Where in the preparation of financial statements, a treatment different from that prescribed in an Accounting Standard has been followed, the fact shall be disclosed in the financial statements, together with the management's explanation as to why it believes such alternative treatment is more representative of the true and fair view of the underlying business</p>	<p>Section 129(5)</p> <p>Where the financial statements of a company do not comply with the accounting standards, the company shall disclose in its financial statements, the deviation from the accounting standards, the reasons for such deviation and the financial effects, if any, arising out of such deviation.</p>

		transaction in the Corporate Governance Report.	
22.	Disclosure on Remuneration	<p>Regulation 34(3)</p> <ol style="list-style-type: none"> 1. All pecuniary relationship or transactions of the non-executive director's vis-à-vis the Listed Entity shall be disclosed in the Annual Report. 2. In addition to the disclosures required under the Companies Act, 2013, the following disclosures on the remuneration of directors shall be made in the section on the corporate governance of the Annual Report: <ol style="list-style-type: none"> (a) All elements of remuneration package of individual directors summarized under major groups, such as salary, benefits, bonuses, stock options, pension etc. (b) Details of fixed component and performance linked incentives, along with the performance criteria. (c) Service contracts, notice period, severance fees. (d) Stock option details, if any – and whether issued at a discount as well as the period over which accrued and over which exercisable. 3. The Listed Entity shall publish its criteria of making payments to non-executive directors in its annual report. Alternatively, this may be put up on the Listed Entity website and reference drawn thereto in the annual report. 4. The Listed Entity shall disclose the number of shares and convertible instruments held by non-executive directors in the annual report. 5. Non-executive directors shall be required to disclose their 	<p>Section 197 and Rule 5 of Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014</p> <p>(1) Every listed company shall disclose in the Board's report:</p> <ol style="list-style-type: none"> (i) The ratio of the remuneration of each director to the median remuneration of the employees of the company for the financial year. (ii) the percentage increase in remuneration of each director, CFO, CEO, CS or Manager, if any, in the financial year; (iii) the percentage increase in the median remuneration of employees in the financial year; (iv) the number of permanent employees on the rolls of company; (v) the explanation on the relationship between average increase in remuneration and company performance; (vi) comparison of the remuneration of the KMP against the performance of the company; (vii) variations in the market capitalisation of the company, price earnings ratio as at the closing date of the current financial year and previous financial year and percentage increase over company came out with the last public offer in case of listed companies, and in case of unlisted companies, the variations in the net worth of the company as at the close of the current financial year and previous financial year; (viii) average percentile increase already made in the salaries of employees other than the managerial personnel in the last financial year and its comparison with the percentile increase in the managerial remuneration and justification thereof and point out if there are any exceptional circumstances for increase in the managerial remuneration;

		<p>shareholding (both own or held by / for other persons on a beneficial basis) in the Listed Entity in which they are proposed to be appointed as directors, prior to their appointment. These details should be disclosed in the notice to the general meeting called for appointment of such director.</p>	<p>(ix) Comparison of the each remuneration of the Key Managerial personnel against the performance of the company.</p> <p>(x) the key parameters for any variable component of remuneration availed by the directors;</p> <p>(xi) the ratio of the remuneration of the highest paid director to that of the employees who are not directors but receive remuneration in excess of the highest paid director during the year; and</p> <p>(xii) Affirmation that the remuneration is as per the remuneration policy of the company.</p>
23.	Stakeholders Relationship Committee	<p>Regulation 20</p> <p>A committee under the Chairperson of a non-executive director and such other members as may be decided by the Board of directors of the Listed Entity shall be formed to specifically look into the redressal of grievances of shareholders, debenture holders and other security holders. This Committee shall be designated as 'Stakeholders Relationship Committee' and shall consider and resolve the grievances of the security holders of the Listed Entity including complaints related to transfer of shares, non-receipt of balance sheet, non-receipt of declared dividends.</p>	<p>Section- 178(5)&(6)</p> <p>The Board of Directors of a company which consists of more than one thousand shareholders, debenture-holders, deposit holders and any other security holders at any time during a financial year shall constitute a Stakeholders Relationship Committee consisting of a chairperson who shall be a non-executive director and such other members as may be decided by the Board. The Stakeholders Relationship Committee shall consider and resolve the grievances of security holders of the company.</p>

DELISTING

The term "delisting" of securities means permanent removal of securities of a listed company from a stock exchange. As a consequence of delisting, the securities of that company would no longer be traded at that stock exchange. Delisting can be Voluntary or Compulsory.

In its continuous endeavour, SEBI in the year 2002 constituted a committee on delisting of shares to inter-alia examine and review the conditions for delisting of securities of companies listed on recognized stock exchanges and suggest norms and procedures in connection therewith. The Report of the Committee was considered and accepted by SEBI. Pursuant to the same, SEBI issued the SEBI (Delisting of Securities) Guidelines, 2003.

The said Guidelines, although, to a great extent covered the issues involved in Delisting of Securities. However, there were certain areas over which hue and cry was made from various quarters. Various representations and

views, from intermediaries, stock exchanges, shareholders' associations, chambers of commerce, etc., were given to the Regulators on the operational issues and procedural complications in the guidelines. Based on such representations, it was proposed to look into and suggest changes in the guidelines. In the month of April 2004, the initial changes proposing more systemic clarity were put up for public comments. Comments were received from various quarters and opinions were received on crucial provisions. SEBI circulated Concept Paper on the proposed SEBI (Delisting of Securities) Regulations, 2006, asking for public comments on the proposed Regulations. SEBI received various comments, opinions and suggestions on the subject and finally, by its publication dated 10th June 2009 in the Official Gazette, SEBI notified the SEBI (Delisting of Equity Shares) Regulations, 2009.

DIFFERENCE BETWEEN COMPULSORY AND VOLUNTARY DELISTING

Compulsory delisting refers to permanent removal of securities of a listed company from a stock exchange as a penalizing measure at the behest of the stock exchange for not making submissions/comply with various requirements set out in the Listing agreement within the time frames prescribed. In voluntary delisting, a listed company decides on its own to permanently remove its securities from a stock exchange.

SEBI in exercise of the powers conferred by Section 31 read with Section 21A of the Securities Contracts (Regulation) Act, 1956, Section 30, sub-section (1) of Section 11 and sub-section (2) of Section 11A of SEBI Act, 1992 made the SEBI (Delisting of Equity Shares) Regulations, 2009.

SEBI (DELISTING OF EQUITY SHARES) REGULATIONS, 2009

APPLICABILITY

Delisting of equity shares of a company from all or any of the recognised stock exchanges where such shares are listed.

NON-APPLICABILITY

These regulation shall not be applicable to securities listed without making a public issue, on the institutional trading platform of a recognised stock exchange and under a scheme sanctioned by the Board for Industrial and Financial Reconstruction under the Sick Industrial Companies (Special Provisions) Act, 1985 or by the National Company Law Tribunal under section 262 of the Companies Act, 2013*, if such scheme lays down any specific procedure to complete the delisting; or provides an exit option to the existing public shareholders at a specified rate.

IMPORTANT DEFINITIONS

Public Shareholder

Public Shareholders have been defined as the holders of equity shares, other than the following:

- (a) promoters;
- (b) holders of depository receipts issued overseas against equity shares held with a custodian and such custodian;

Person Acting in Concert (PAC)

The term PAC shall have the same meaning as assigned to it under the SEBI (SAST) Regulations, 2011. PACs are individual(s) /company(ies)/ any other legal entity(ies) who are acting together for a common objective or for a purpose of substantial acquisition of shares or voting rights or gaining control over the target company pursuant to an agreement or understanding whether formal or informal. Acting in concert would imply co-operation, co-ordination for acquisition of voting rights or control. This co-operation/ co-ordinated approach may either be direct or indirect.

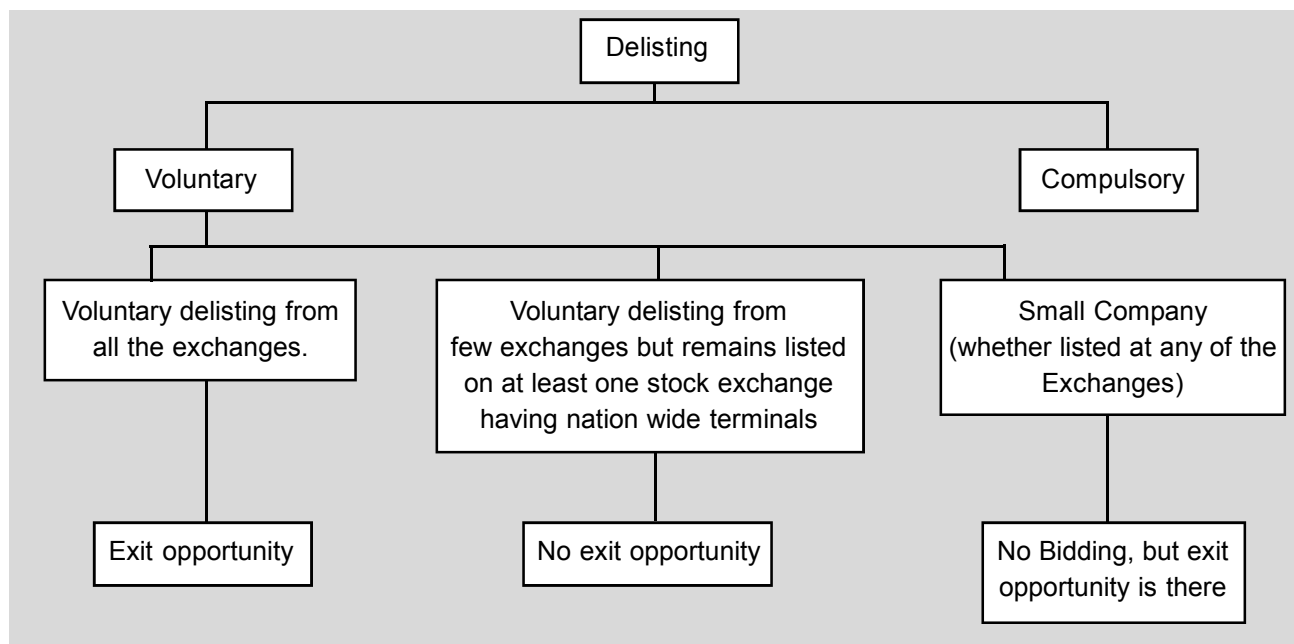
Unless the contrary is established certain entities are deemed to be persons acting in concert like companies with its holding company or subsidiary company, mutual funds with its sponsor / trustee/ Asset management company, etc.

CIRCUMSTANCES WHERE DELISTING IS NOT PERMISSIBLE

- In case of buy back of equity shares by the company; or
- In case of preferential allotment made by the company; or
- Unless a period of three years has elapsed since the listing of that class of equity shares on any recognised stock exchange; or
- Instruments which are convertible into the same class of equity shares that are sought to be delisted are outstanding.
- No promoter or promoter group shall propose delisting of equity shares of company, if any entity belonging to the promoter or promoter group has sold equity shares of the company during a period of six month prior to the date of the Board meeting in which the delisting proposal was approved.
- Delisting of convertible securities.
- No promoter shall directly or indirectly employ the funds of the company to finance an exit opportunity or an acquisition of shares made pursuant to provided under these regulation.
- No acquirer or promoter or promoter group or their related entities shall.
- Employ any device, scheme or artifice to defraud any shareholder or other person; or
- Engage in any transaction or practice that operates as a fraud or deceit upon any shareholder or other person; or
- Engage in any act or practice that is fraudulent, deceptive or manipulative in connection with such delisting.

VOLUNTARY DELISTING**DELISTING FROM ALL RECOGNISED STOCK EXCHANGES**

A company may delist its equity shares from all or from the only recognised stock exchange where they are listed. However, all public shareholders holding equity shares of the class which are sought to be delisted are given an exit opportunity in accordance with these regulations.



PUBLIC ANNOUNCEMENT

- The acquirers or promoters of the company shall within one working day from the date of receipt of in-principle approval for delisting from the recognised stock exchange, make a public announcement which contains all material information and shall not contain any false or misleading statement, in at least one English national daily with wide circulation, one Hindi national daily with wide circulation and one regional language newspaper of the region where the concerned recognised stock exchange is located.
- The public announcement shall also specify a date, being a day not later than thirty working days from the date of the public announcement, which shall be the 'specified date' for determining the names of shareholders to whom the letter of offer shall be sent.
- Before making the public announcement, the promoter shall appoint a merchant banker registered with SEBI and such other intermediaries as are considered necessary to ensure compliance with these regulations.
- No acquirer/promoter shall appoint any person as a merchant banker if such a person is an associate of the promoter.
- No entity belonging to the acquirer, promoter and promoter group of the company shall shares of the company during the period from the date of board making in which the delisting proposal was approved till the completion of the delisting process.

ESCROW ACCOUNT

- Before making the public announcement the acquirer or promoter shall open an escrow account and deposit therein the total estimated amount of consideration calculated on the basis of floor price and number of equity shares outstanding with public shareholders.
- On determination of final price the acquirer or promoter shall forthwith deposit in the escrow account such additional sum as may be sufficient to make up the entire sum due and payable as consideration in respect of equity shares outstanding with public shareholders.
- The escrow account shall consist of either cash deposited with a scheduled commercial bank, or a bank

guarantee in favour of the merchant banker, or a combination of both.

LETTER OF OFFER

- The acquirer or promoter shall despatch the letter of offer to the public shareholders of equity shares, not later than two working days from the date of the public announcement.
- The letter of offer shall be sent to all public shareholders whose names appear on the register of the company or depository as on the date specified in the public announcement .
- The letter of offer shall contain all the disclosures made in the public announcement and such other disclosures as may be necessary for the shareholders to take an informed decision.
- The letter of offer shall be accompanied with a bidding form for use of public shareholders and a form to be used by them for tendering shares.

BIDDING PERIOD

- The date of opening of the offer shall not be later than seven working days from the date of the public announcement.
- The acquirer or promoter shall facilitate tendering of shares by the shareholders and settlement of the same, through the stock exchange mechanism.
- The offer shall remain open for a minimum period of three working days and a maximum period of five working days.

RIGHT OF SHAREHOLDER

- All public shareholders of the equity shares which are sought to be delisted shall be entitled to participate in the book building process.
- An acquirer or promoter or a person acting in concert with any of the promoters shall not make a bid in the offer.
- Any holder of depository receipts issued on the basis of underlying shares held by a custodian and any such custodian shall not be entitled to participate in the offer and this shall not affect if the holder of depository receipts exchanges such depository receipts with shares of the class that are proposed to be delisted.

OFFER PRICE

The offer price shall be determined through book building process after fixation of floor price and disclosure of the same in the public announcement and the letter of offer.

The floor price shall be determined in terms of SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011, as may be applicable.

RIGHT OF PROMOTER NOT TO ACCEPT THE OFFER PRICE

The acquirer or promoter is not bound to accept the equity shares at the offer price determined by the book building process. If the acquirer or promoter decides not to accept the offer price so determined,—

- (a) the acquirer or promoter shall not acquire any equity shares tendered pursuant to the offer and the equity shares deposited or pledged by a shareholder shall be returned or released to him within ten working days of closure of the bidding period;
- (b) the company shall not make the final application to the exchange for delisting of the equity shares;

- (c) the acquirer or promoter may close the escrow account.

MINIMUM NUMBER OF EQUITY SHARES TO BE ACQUIRED

An offer made shall be deemed to be successful only if,-

- (a) the post offer promoter shareholding (along with the persons acting in concert with the promoter) taken together with the shares accepted through eligible bids at the final price determined as per Schedule II, reaches ninety per cent of the total issued shares of that class excluding the shares which are held by a custodian and against which depository receipts have been issued overseas; and
- (b) at least twenty five per cent of the public shareholders holding shares in the demat mode as on date of the board meeting had participated in the Book Building Process.

However, this requirement shall not be applicable to cases where the acquirer and the merchant banker demonstrate to the stock exchanges that they have delivered the letter of offer to all the public shareholders either through registered post or speed post or courier or hand delivery with proof of delivery or through email as a text or as an attachment to email or as a notification providing electronic link or Uniform Resource Locator including a read receipt.

Explanation.- In case the delisting offer has been made in terms of regulation 5A of the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011, the threshold limit of ninety per cent for successful delisting offer shall be calculated taking into account the post offer shareholding of the acquirer taken together with the existing shareholding, shares to be acquired which attracted the obligation to make an open offer and shares accepted through eligible bids at the final price determined as per Schedule II.

CLOSURE OF OFFER

Within five working days of closure of the offer, the acquirer or promoter and the merchant banker shall make a public announcement in the newspapers regarding:-

- (i) the success of the offer along with the final price accepted by the acquirer; or
- (ii) the failure of the offer; or
- (iii) rejection of the final price discovered under Schedule II, by the promoters.

FAILURE OF OFFER

(1) Where the offer is rejected or is not successful as, the offer shall be deemed to have failed and no equity shares shall be acquired pursuant to such offer.

(2) Where the offer fails –

- (a) the equity shares deposited or pledged by a shareholder shall be returned or released to him within ten working days from the end of the bidding period;

However, the acquirer shall not be required to return the shares if the offer is made pursuant to regulation 5A of SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011.

- (b) no final application shall be made to the exchange for delisting of the equity shares; and
- (c) the escrow account opened shall be closed.

PAYMENT OF CONSIDERATION

1. The promoter shall immediately on ascertaining success of the offer, open a special account with a banker to an issue registered with SEBI and transfer thereto, the entire amount due and payable as consideration in respect of equity shares tendered in the offer, from the escrow account.

2. All the shareholders whose equity shares are verified to be genuine shall be paid the final price stated in the public announcement within ten working days from the closure of the offer.

RETURN OF EQUITY SHARES

The equity shares deposited or pledged by a shareholder shall be returned or released to him, within ten working days from the closure of the offer, in cases where the bids pertaining thereto have not been accepted.

RIGHT OF REMAINING SHAREHOLDERS TO TENDER EQUITY SHARES

- (1) Where, pursuant to acceptance of equity shares tendered in terms of these regulations, the equity shares are delisted, any remaining public shareholder holding such equity shares may tender his shares to the promoter upto a period of at least one year from the date of delisting and, in such a case, the promoter shall accept the shares tendered at the same final price at which the earlier acceptance of shares was made.
- (2) The payment of consideration for shares accepted shall be made out of the balance amount lying in the escrow account.
- (3) The amount in the escrow account or the bank guarantee shall not be released to the promoter unless all payments are made in respect of shares tendered.

DELISTING FROM ONLY SOME OF THE RECOGNISED STOCK EXCHANGES

A company may delist its equity shares from one or more recognised stock exchanges where they are listed and continue their listing on one or more other recognised stock exchanges, if after the proposed delisting the equity shares would –

- remain listed on any recognised stock exchange which has nationwide trading terminals, no exit opportunity needs to be given to the public shareholders; and,
- not remain listed on any recognised stock exchange having nation wide trading terminals, exit opportunity shall be given to all the public shareholders holding the equity shares sought to be delisted.

‘Recognised stock exchange having nation wide trading terminals’ means the Bombay Stock Exchange Limited, the National Stock Exchange of India Limited or any other recognised stock exchange which may be specified by SEBI in this regard.’

PROCEDURE FOR DELISTING

In case of no exit opportunity

- (1) It shall be approved by a resolution of the board of directors of the company in its meeting;
- (2) The company shall give a public notice of the proposed delisting in at least one English national daily with wide circulation, one Hindi national daily with wide circulation and one regional language newspaper of the region where the concerned recognised stock exchanges are located.
- (3) The company shall make an application to the concerned recognised stock exchange regarding this.
- (4) The fact of delisting shall be disclosed in the first annual report of the company prepared after the delisting.
- (5) The public notice shall mention the names of the recognised stock exchanges from which the equity shares of the company are intended to be delisted, the reasons for such delisting and the fact of continuation of listing of equity shares on recognised stock exchange having nation wide trading terminals.
- (6) An application shall be disposed off by the recognised stock exchange within a period not exceeding thirty working days from the date of receipt of such application complete in all respects.

In case of exit opportunity

Except where the equity shares would remain listed on any recognised stock exchange which has nationwide trading terminals and no exit opportunity needs to be given to the public shareholders, any company desirous of delisting its equity shares –

- (1) Obtain the prior approval of the board of directors of the company in its meeting;
- (2) Obtain the prior approval of shareholders of the company by special resolution passed through postal ballot, after disclosure of all material facts in the explanatory statement sent to the shareholders in relation to such resolution. However, the special resolution shall be acted upon if and only if the votes cast by public shareholders in favour of the proposal amount to at least two times the number of votes cast by public shareholders against it.
- (3) Make an application to the concerned recognised stock exchange for in-principle approval of the proposed delisting.
- (4) An application shall be disposed off by the recognised stock exchange within a period not exceeding five working days from the date of receipt of such application complete in all respects.
- (5) within one year of passing the special resolution, make the final application to the concerned recognised stock exchange in the form specified by the recognised stock exchange.

However, in pursuance of special resolution, passed before the commencement of these regulations, final application shall be made within a period of one year from the date of passing of special resolution or six months from the commencement of these regulations, whichever is later.

- (6) Prior to granting approval, the board of directors of the company shall,-
 - (i) make a disclosure to the recognized stock exchanges on which the equity shares of the company are listed that the promoters/acquirers have proposed to delist the company;
 - (ii) appoint a merchant banker to carry out due-diligence and make a disclosure to this effect to the recognized stock exchanges on which the equity shares of the company are listed;
 - (iii) obtain details of trading in shares of the company for a period of two years prior to the date of board meeting by top twenty five shareholders as on the date of the board meeting convened to consider the proposal for delisting, from the stock exchanges and details of off-market transactions of such shareholders for a period of two years and furnish the information to the merchant banker for carrying out due-diligence;
 - (iv) obtain further details and furnish the information to the merchant banker.
- (7) The board of directors of the company while approving the proposal for delisting shall certify that :
 - (i) the company is in compliance with the applicable provisions of securities laws;
 - (ii) the acquirer or promoter or promoter group or their related entities, are in compliance with sub-regulation (5) of regulation 4;
 - (iii) the delisting is in the interest of the shareholders.
- (8) For certification as mentioned above, the board of directors of the company shall take into account the report of the merchant banker.
- (9) The merchant banker appointed by the board of directors of the company shall carry out due diligence upon obtaining details from the board of directors of the company.

However, if the merchant banker is of the opinion that details referred above are not sufficient for

certification, he shall obtain additional details from the board of directors of the company for such longer period as he may deem fit.

- (10) Upon carrying out due-diligence as specified in these regulations, the merchant banker shall submit a report to the board of directors of the company certifying the following:
 - (a) the trading carried out by the entities belonging to acquirer or promoter or promoter group or their related entities was in compliance or not, with the applicable provisions of the securities laws; and
 - (b) entities belonging to acquirer or promoter or promoter group or their related entities have carried out or not, any transaction to facilitate the success of the delisting offer which is not in compliance with the provisions of sub-regulation (5) of regulation 4.
- (11) An application seeking in-principle approval for delisting shall be accompanied by an audit report as required under regulation 55A of SEBI (Depositories and Participants) Regulations, 1996 in respect of the equity shares sought to be delisted, covering a period of six months prior to the date of the application.
- (12) The recognised stock exchange shall not unfairly withhold such application, but may require the company to satisfy it as to –
 - (a) Compliance with these regulations
 - (b) The resolution of investor grievances by the company;
 - (c) Payment of listing fees to that recognised stock exchange;
 - (d) The compliance with any condition of the listing agreement with that recognised stock exchange having a material bearing on the interests of its equity shareholders;
 - (e) Any litigation or action pending against the company pertaining to its activities in the securities market or any other matter having a material bearing on the interests of its equity shareholders;
 - (f) Any other relevant matter as the recognised stock exchange may deem fit to verify.
- (13) Within one year of passing the special resolution, make the final application to the concerned recognised stock exchange in the form specified by the recognised stock exchange and shall be accompanied with such proof of having given the exit opportunity in accordance with these regulations as the recognised stock exchange may require.

SPECIAL PROVISIONS FOR SMALL COMPANIES AND DELISTING BY OPERATION OF LAW

Equity shares of a company may be delisted from all the recognised stock exchanges where they are listed, if,-

- (a) the company has a paid up capital not exceeding ten crore rupees and net worth not exceeding twenty five crore rupees as on the last date of preceding financial year;
- (b) the number of equity shares of the company traded on each such recognised stock exchange during the twelve calendar months immediately preceding the date of board meeting is less than ten per cent of the total number of shares of such company.

However, where the share capital of a particular class of shares of the company is not identical throughout such period, the weighted average of the shares of such class shall represent the total number of shares of such class of shares of the company; and

- (c) the company has not been suspended by any of the recognised stock exchanges having nationwide trading terminals for any non-compliance in the preceding one year;

A delisting of equity shares may be made only if, in addition to the fulfillment of requirement where exit opportunity is required, the following conditions are fulfilled:-

- (a) the promoter appoints a merchant banker and decides an exit price in consultation with him;
- (b) the exit price offered to the public shareholders shall not be less than the floor price;
- (c) the promoter writes individually to all public shareholders in the company informing them of his intention to get the equity shares delisted, indicating the exit price together with the justification therefor and seeking their consent for the proposal for delisting;
- (d) at least ninety per cent of such public shareholders give their positive consent in writing to the proposal for delisting, and have consented either to sell their equity shares at the price offered by the promoter or to remain holders of the equity shares even if they are delisted;
- (e) the promoter completes the process of inviting the positive consent and finalisation of the proposal for delisting of equity shares within seventy five working days of the first communication made by the promoter individually to all public shareholders;
- (f) the promoter makes payment of consideration in cash within fifteen working days from the date of expiry of seventy five working days stipulated .

The communication made to the public shareholders shall contain justification for the offer price with particular reference to the applicable parameters for offer price, that consent for the proposal would include consent for dispensing with the exit price discovery through book building method.

The concerned recognised stock exchange may delist such equity shares upon satisfying itself of compliance with this regulation.

IN CASE OF WINDING UP, DERECOGNITION

In case of winding up proceedings of a company whose equity shares are listed on a recognised stock exchange, the rights, if any, of the shareholders of such company shall be in accordance with the laws applicable to those proceedings.

Where SEBI withdraws recognition granted to a stock exchange or refuses renewal of recognition to it, SEBI may, in the interest of investors pass appropriate order in respect of the status of equity shares of the companies listed on that exchange.

MONITORING COMPLIANCES

The respective recognised stock exchanges shall comply with and monitor compliance with the provisions of these regulations and shall report to SEBI any instance of non-compliance which comes to their notice.

LISTING OF DELISTED EQUITY SHARES

An application for listing shall not be made in respect of any equity shares:

- (a) which have been delisted under voluntary delisting or by operation of law except delisting of small companies, for a period of five years from the delisting.
- (b) which have been delisted under compulsory delisting, for a period of ten years from the delisting.

However, this shall not be applicable where a recommendation for listing has been made by SEBI for Industrial and Financial Reconstruction under the Sick Industrial Companies (Special Provisions) Act, 1985.

While considering an application for listing of any equity shares which had been delisted the recognised stock exchange shall have due regard to facts and circumstances under which delisting was made.

An application for listing made in respect of delisted equity shares shall be deemed to be an application for fresh listing of such equity shares and shall be subject to provisions of law relating to listing of equity shares of unlisted companies.

COMPULSORY DELISTING

Compulsory Delisting means permanent removal of securities of a listed company from a stock exchange as a penalizing measure at the behest of the stock exchange for not making submissions/ complying with various requirements set out in the Listing agreement within the time frames prescribed.

BY STOCK EXCHANGE

A recognised stock exchange may, by order, delist any equity shares of a company on any ground prescribed in the rules made under section 21A of the Securities Contracts (Regulation) Act, 1956.

However, no order shall be made under this sub-regulation unless the company concerned has been given a reasonable opportunity of being heard.

The decision on delisting shall be taken by a panel to be constituted by the recognised stock exchange consisting of –

- (a) two directors of the recognised stock exchange (one of whom shall be a public representative);
- (b) one representative of the investors;
- (c) one representative of the Ministry of Corporate Affairs or Registrar of Companies; and
- (d) the Executive Director or Secretary of the recognised stock exchange.

Before making an order the recognised stock exchange shall give a notice in one English national daily with wide circulation and one regional language newspaper of the region where the concerned recognised stock exchange is located, of the proposed delisting, giving a time period of not less than fifteen working days from the notice, within which representations may be made to the recognised stock exchange by any person who may be aggrieved by the proposed delisting and shall also display such notice on its trading systems and website.

The provisions related to exit opportunity shall not be applicable to a compulsory delisting made by a recognised stock exchange under this Chapter.

Where the recognised stock exchange passes an order it shall, –

- (a) forthwith publish a notice in one English national daily with wide circulation and one regional language newspaper of the region where the concerned recognised stock exchange is located, of the fact of such delisting, disclosing therein the name and address of the company, the fair value of the delisted equity shares determined and the names and addresses of the promoters of the company who would be liable under these regulations and
- (b) inform all other stock exchanges where the equity shares of the company are listed, about such delisting and the surrounding circumstances.

The recognised stock exchange shall while passing any order consider the representations, if any, made by the company as also any representations received in response to the notice given and shall comply with the criteria specified in Schedule III which is given below –

SCHEDULE III

CRITERIA FOR COMPULSORY DELISTING

1. The recognised stock exchange shall take all reasonable steps to trace the promoters of a company whose equity shares are proposed to be delisted, with a view to ensuring compliance with sub-regulation (3) of regulation 23.
2. The recognised stock exchange shall consider the nature and extent of the alleged non-compliance of

the company and the number and percentage of shareholders who may be affected by such non-compliance.

3. The recognised stock exchange shall take reasonable efforts to verify the status of compliance of the company with the office of the concerned Registrar of Companies.
4. The names of the companies whose equity shares are proposed to be delisted and their promoters shall be displayed in a separate section on the website of the recognised stock exchange for a brief period of time. If delisted, the names shall be shifted to another separate section on the website.
5. The recognised stock exchange shall in appropriate cases file prosecutions under relevant provisions of the Securities Contracts (Regulation) Act, 1956 or any other law for the time being in force against identifiable promoters and directors of the company for the alleged non-compliances.
6. The recognised stock exchange shall in appropriate cases file a petition for winding up the company under section 271 of the Companies Act, 2013 or make a request to the Registrar of Companies to strike off the name of the company from the register under section 248 of the Companies Act, 2013.

RIGHTS OF PUBLIC SHAREHOLDERS

Where equity shares of a company are delisted by a recognised stock exchange the recognised stock exchange shall appoint an independent valuer or valuers who shall determine the fair value of the delisted equity shares which the promoter of the company pay to the shareholder from the delisted shares are acquired subject to their option of retaining their shares.

The recognised stock exchange shall form a panel of expert valuers from whom the valuer or valuers shall be appointed.

The promoter of the company shall acquire delisted equity shares from the public shareholders by paying them the value determined by the valuer subject to prior option of retaining their shares.

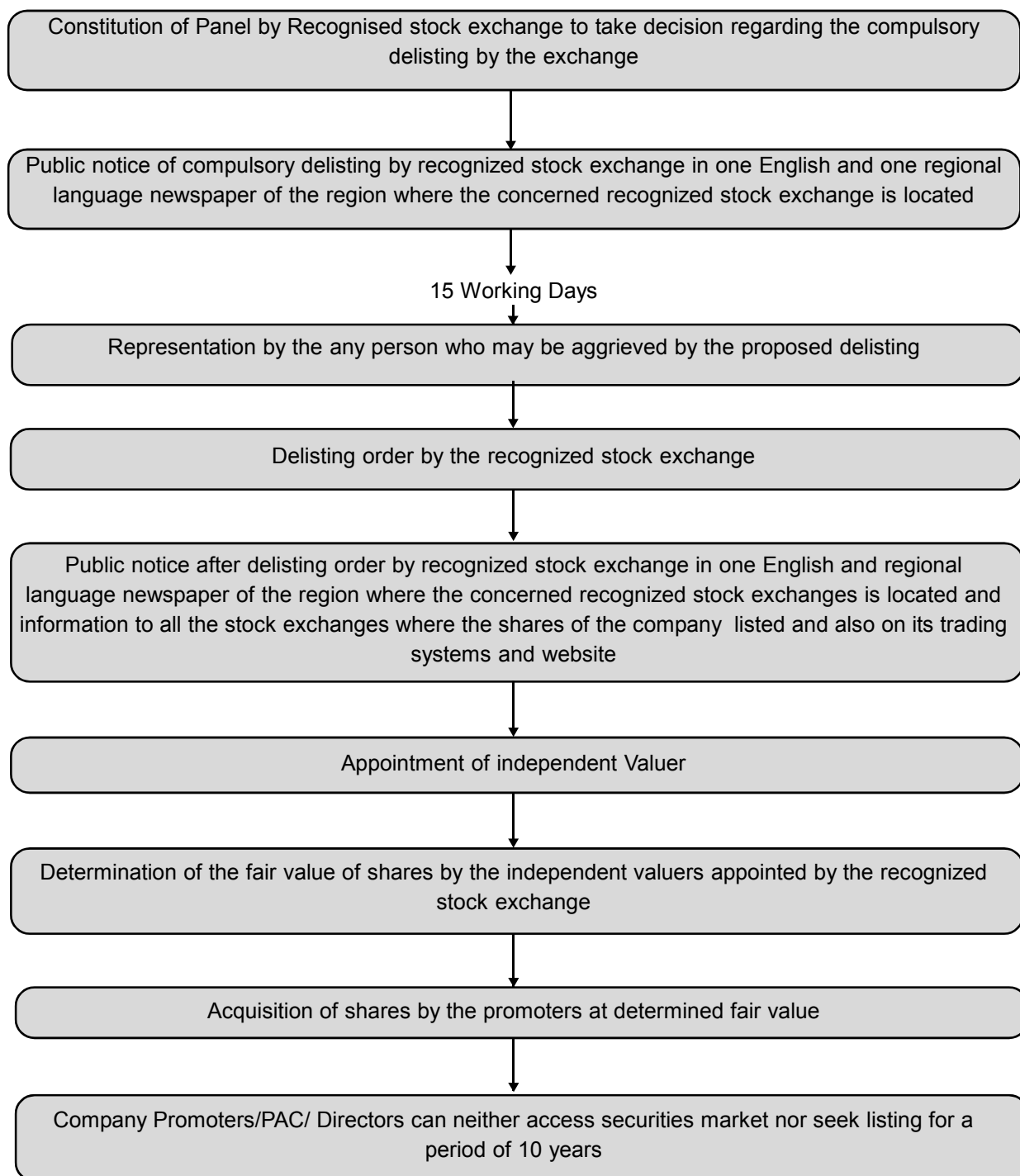
CONSEQUENCES

Where a company has been compulsorily delisted the company, its whole time directors, its promoters and the companies which are promoted by any of them shall not directly or indirectly access the securities market or seek listing for any equity shares for a period of ten years from the date of such delisting.

In addition to the restriction imposed above, in order to ensure effective enforcement of exit option to the public shareholders in case of compulsory delisting and taking into account the interests of investors, it is felt necessary to strengthen the regulatory mechanism in this regard. Accordingly, it is hereby directed that in case of such companies whose fair value is positive:-

- such a company and the depositories shall not effect transfer, by way of sale, pledge, etc., of any of the equity shares and corporate benefits like dividend, rights, bonus shares, split, etc. shall be frozen, for all the equity shares, held by the promoters/ promoter group till the promoters of such company provide an exit option to the public shareholders in compliance with regulation 23(3) of the Delisting Regulations, as certified by the concerned recognized stock exchange;
- the promoters and whole-time directors of the compulsorily delisted company shall also not be eligible to become directors of any listed company till the exit option.

PROCESS FLOW CHART FOR COMPULSORY DELISTING



LESSON ROUND UP

- Listing of securities with stock exchange is a matter of great importance for companies and investors, because this provides the liquidity to the securities in the market.
- Listing of Securities on Indian Stock Exchanges, thus, is essentially governed by the provisions in the Companies Act, 2013, the Securities Contracts (Regulation) Act, 1956, the Securities Contracts (Regulation) Rules, 1957, Rules, bye laws, regulations of concerned stock exchange, and circulars/

guidelines issued by the Central Government and SEBI.

- The listed entity which has listed its specified securities shall comply with the corporate governance provisions as specified in these regulations.
- The Board of directors shall have an optimum combination of executive and non-executive directors with at least one women director and not less than 50% of the BoDs shall comprise of non-executive directors.
- A listed entity shall appoint a qualified company secretary as a compliance officer.
- The term delisting of securities means permanent removal of securities of a listed company from a stock exchange. As a consequence of delisting, the securities of that company would no longer be traded at that stock exchange.
- Delisting can be voluntary or compulsory.

GLOSSARY

Financial year	It means the period of twelve months commencing on the first day of April every year. However, a company may at its option have a financial year commencing on a date other than the first day of April.
Listing Agreement	An agreement which has to be entered into by companies when they such listing for their shares on a stock exchange, companies are called upon to keep the stock exchange fully informed of all corporate developments having a bearing on the market price of shares like dividend rights, bonus shares, etc.
Record Date	A date on which the records of a company are closed for the purpose of determining the stock-holders to whom dividends, proxies rights etc., are to be sent.
Material subsidiary	It means a subsidiary, whose income or net worth exceeds 20% of the consolidated income or net worth respectively, of the listed entity and its subsidiaries in the immediately preceding accounting years.

SELF TEST QUESTIONS

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation.)

1. Listing of securities with stock exchange is a matter of great importance for companies and investors'. Discuss.
2. What are the timelines for submission of disclosures relating to each class of equity shares/ security issued under Regulation 31 of SEBI (LODR), 2015?
3. Briefly explain the provision related to composition of Board of Director under Regulation 17 of the SEBI (LODR), 2015?
4. What is the duty of Compliance officer under Regulation 6 of the SEBI (LODR), 2015?
5. Distinguish between voluntary delisting of securities and compulsory delisting of securities.
6. Briefly explain the procedure for voluntary delisting only from some of the stock exchange.
7. Discuss corporate governance provisions under SEBI (LODR), 2015
8. Explain the provisions related to "in-principle approval" of recognised stock exchange under Regulation 25 of SEBI (LODR), 2015
9. Discuss corporate governance provisions under SEBI (LODR), 2015.

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Lesson 20

Issue of Securities

LESSON OUTLINE

- Introduction
- Issue of Equity Shares
- Meaning of Draft offer document, Letter of offer and Red Herring Prospectus
- Fast Track Issues
- Pricing
- Promoters' Contribution
- Lock-in Requirements
- Underwriting
- Reservation on competitive basis
- Allocation in net offer to public
- Book Building
- Anchor Investors
- Application Supported by Block Amount (ASBA)
- Green Shoe Option facility
- Procedure for Issue of Securities
- Rights issue
- Bonus Shares
- Preferential Issue by Existing Listed Companies
- Qualified Institutional Placement
- Institutional Placement Programme
- Listing on Institutional Trading Platform
- Issue of Securities by SME
- Listing of Securities on Stock Exchange
- Exit Opportunity to Dissenting Shareholders
- SEBI (Share Based Employee Benefits) Regulations, 2014
- LESSON ROUND-UP
- GLOSSARY
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

The Indian stock market witnessed transformation after the opening up of the economy in the early nineties, especially after the establishment of SEBI. The companies are also raising funds through new avenues to fulfill its fund requirement for different purpose. SEBI regulates the issue of securities by listed public companies in India by SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009 (ICDR Regulations), that regulates various types of issues relating to aspects such as eligibility, Promoters' Contribution, Pricing and other Procedural aspects.

This lesson will enable the students to learn the various provisions of SEBI (ICDR) Regulations, 2009 in respect of various types of issues, such as IPO/FPO, Rights Issue, Bonus Issue, Preferential Issue, Issue of Advertisements, Promoters' Contributions, Lock-in requirements, Green Shoe Option, Book Building Method, Issue of QIPs, Institutional Placement Programme, ESOP Guidelines, etc.

INTRODUCTION

Management of a public issue involves coordination of activities and cooperation of a number of agencies such as managers to the issue, underwriters, brokers, registrar to the issue; solicitors/legal advisors, printers, publicity and advertising agents, financial institutions, auditors and other Government/Statutory agencies such as Registrar of Companies, Reserve Bank of India, SEBI etc. The whole process of issue of shares can be divided into two parts (i) pre-issue activities and (ii) post issue activities. All activities beginning with the planning of capital issue till the opening of the subscription list are pre-issue activities while all activities subsequent to the opening of the subscription list may be called post issue activities. Since only the demat shares are being admitted for dealings on the stock exchanges, hence the securities can be issued only with the purpose of allotting the shares in Dematerialised Form.

With the repeal of Capital Issues (Control) Act, 1947 all the guidelines, notifications, circulars etc. issued by the office of the Controller of Capital Issues have become defunct. Earlier, such companies were required to conform to the guidelines issued by SEBI vide its order dated 11.6.1992 called the Guidelines for Disclosure and Investor Protection, 1992.

SEBI had issued a compendium containing consolidated Guidelines, circulars, instructions relating to issue of capital effective from January 27, 2000. The compendium titled SEBI (Disclosure and Investor Protection) Guidelines, 2000 replaced the original Guidelines issued in June 1992 and clarifications thereof. On August 26, 2009 SEBI rescinded the SEBI (DIP) Guidelines, 2000 and notified SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009 in order to bring more clarity to the provisions of the rescinded SEBI Guidelines by removing the redundant provision and modifying certain provisions on account of changes necessitated due to market design.

ISSUE OF EQUITY SHARES

The important aspects of SEBI (ICDR) Regulations, 2009 with reference to issue of equity shares are as under:

APPLICABILITY OF THE REGULATIONS

These regulations shall apply to the following:

- (a) Public issue;
- (b) Rights issue, where the aggregate value of specified securities offered is fifty lakh rupees or more;
- (c) Preferential issue;
- (d) Issue of bonus shares by a listed issuer;
- (e) Qualified institutions placement by a listed issuer;
- (f) Institutional Placement Programme (IPP); and
- (g) Issue of Indian Depository Receipts.

ELIGIBILITY NORMS FOR PUBLIC ISSUE

Unlisted Company

An unlisted company can make an initial public offering (IPO) of equity shares or any other security which may be converted into or exchanged with equity shares at a later date, only if it meets all the following conditions:

- (a) The company has net tangible assets of at least ₹ 3 crores in each of the preceding 3 full years (of 12 months each), of which not more than 50% is held in monetary assets.

However, if more than 50% 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. Further the limit of 50% on monetary assets shall not be applicable in case the public offer is made entirely through an offer for sale.

- (b) The company has a minimum average pre-tax operating profit of rupees fifteen crore, calculated on a restated and consolidated basis, during the three most profitable years out of the immediately preceding five years.
- (c) The company has a net worth of at least ₹ 1 crore in each of the preceding 3 full years (of 12 months each);
- (d) The aggregate of the proposed issue and all previous issues made in the same financial year in terms of size, does not exceed five (5) times its pre-issue net worth as per the audited balance sheet of the last financial year.
- (e) In case the company has changed its name within the last one year, at least 50% of the revenue for the preceding 1 full year is earned by the company from the activity suggested by the new name; and

Listed Company

A listed company shall be eligible to make a public issue of equity shares or any other security which may be converted into or exchanged with equity shares at a later date: the aggregate of the proposed issue and all previous issues made in the same financial year in terms of size, issue size does not exceed 5 times its pre-issue networth as per the audited balance sheet of the last financial year.

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

ALTERNATIVE ELIGIBILITY NORMS FOR PUBLIC ISSUE

To provide sufficient flexibility and also to ensure that genuine companies do not suffer on account of rigidity of the parameters, SEBI has provided alternative route to company not satisfying any of the above conditions, for accessing the Primary Market, if the issue is made through the book-building process and the issuer undertakes to allot, at least seventy five percent of the net offer to public, to qualified institutional buyers and to refund full subscription money if it fails to make the said minimum allotment to qualified institutional buyers. An issuer shall not make an allotment pursuant to a public issue if the number of prospective allottees is less than one thousand. Further, an issuer shall not make an initial public offer if there are any outstanding convertible securities or any other right which would entitle any person with any option to receive equity shares.

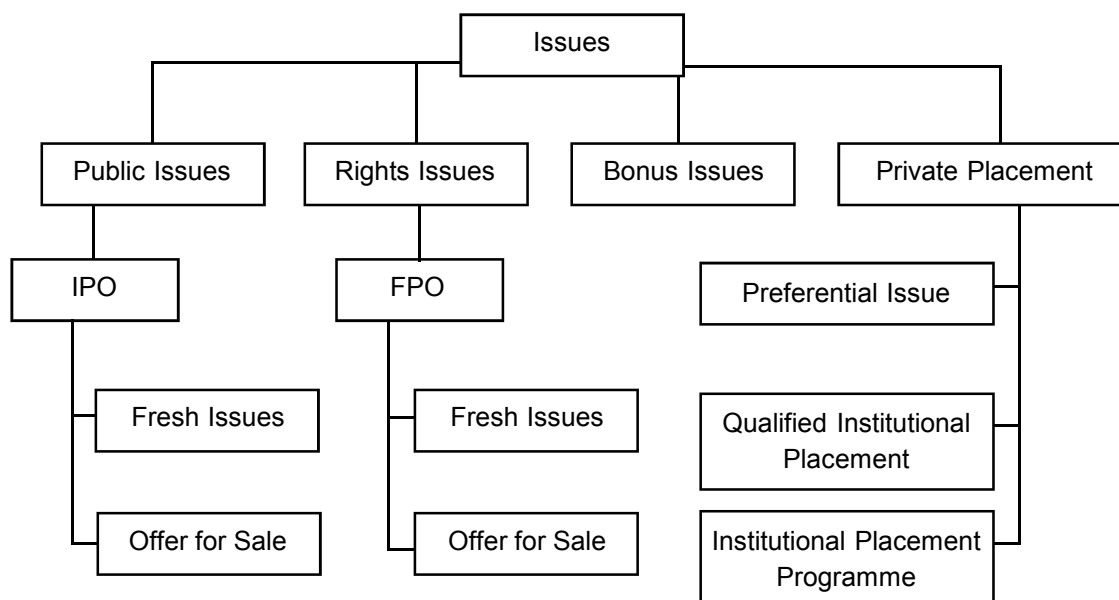
TYPES OF ISSUE

Public Issue of shares means the selling or marketing of shares for subscription by the public by issue of prospectus. For raising capital from the public by the issue of shares, a public company has to comply with the provisions of the Companies Act, the Securities Contracts (Regulation) Act, 1956 including the Rules made thereunder and the guidelines and instructions issued by the concerned Government authorities, the Stock Exchanges and SEBI etc.

A company can raise funds from the primary market through different method:

- (a) **Public issue:** When an issue/offer of securities is made to new investors for becoming part of shareholders' family of the issuer it is called a public issue. Public issue can be further classified into Initial public offer (IPO) and Further public offer (FPO). The significant features of each type of public issue are illustrated below:

- (i) **Initial public offer (IPO):** When an unlisted company makes either a fresh issue of securities or offers its existing securities for sale or both for the first time to the public, it is called an IPO. This paves way for listing and trading of the issuer's securities in the Stock Exchanges.
- (ii) **Further public offer (FPO) or Follow on offer:** When an already listed company makes either a fresh issue of securities to the public or an offer for sale to the public, it is called a FPO.
- (b) **Right issue (RI):** When an issue of securities is made by an issuer to its shareholders existing as on a particular date fixed by the issuer (i.e. record date), it is called a rights issue. The rights are offered in a particular ratio to the number of securities held as on the record date.
- (c) **Bonus issue:** When an issuer makes an issue of securities to its existing shareholders as on a record date, without any consideration from them, it is called a bonus issue. The shares are issued out of the Company's free reserve or share premium account in a particular ratio to the number of securities held on a record date.
- (d) **Private placement:** When an issuer makes an issue of securities to a select group of persons not exceeding 49, and which is neither a rights issue nor a public issue, it is called a private placement. Private placement of shares or convertible securities by listed issuer can be of two types:
- (i) **Preferential allotment:** When a listed issuer issues shares or convertible securities, to a select group of persons in terms of provisions of Chapter VII of SEBI (ICDR) Regulations, it is called a preferential allotment. The issuer is required to comply with various provisions which *inter alia* include pricing, disclosures in the notice, lock in etc., in addition to the requirements specified in the Companies Act, 2013.
- (ii) **Qualified institutions placement (QIP):** When a listed issuer issues equity shares or securities convertible into equity shares to Qualified Institutions Buyers (QIBs) only in terms of provisions of Chapter VIII of SEBI (ICDR) Regulations, it is called a QIP.
- (iii) **Institutional placement programme (IPP):** When a listed issuer makes a further public offer of equity shares, or offer for sale of shares by promoter / promoter group of listed issuer in which, the offer allocation and allotment of such shares is made only to QIBs in terms of chapter VIIIA of SEBI (ICDR) Regulations, 2009 for the purpose of achieving minimum public shareholding it is called an IPP.



MEANING OF DRAFT OFFER DOCUMENT, LETTER OF OFFER AND RED HERRING PROSPECTUS

<i>Draft Offer Documents</i>	<i>Offer Document</i>	<i>RHP (Red Herring Prospectus)</i>
<p>“Draft Offer document” means the offer document in draft stage. The draft offer documents are filed with SEBI, atleast 30 days prior to the filing of the Offer Document with ROC/SEs. SEBI may specifies changes, if any, in the Draft Offer Document and the Issuer or the Lead Merchant banker shall carry out such changes in the draft offer document before filing the Offer Document with ROC/SEs. The Draft Offer document is available on the SEBI website for public comments for a period of 21 days from the filing of the Draft Offer Document with SEBI.</p>	<p>“Offer document” means Prospectus in case of a public issue or offer for sale and Letter of Offer in case of a right issue, which is filed with Registrar of Companies (ROC) and Stock Exchanges. An offer document covers all the relevant information to help an investor to make his/her investment decision.</p>	<p>“Red Herring Prospectus” is a prospectus, which does not have details of either price or number of shares being offered, or the amount of issue. This means that in case price is not disclosed, the number of shares and the upper and lower price bands are disclosed. On the other hand, an issuer can state the issue size and the number of shares are determined later. An RHP for an FPO can be filed with the ROC without the price band and the issuer, in such a case will notify the floor price or a price band by way of an advertisement one day prior to the opening of the issue. In the case of book-built issues, it is a process of price discovery and the price cannot be determined until the bidding process is completed. Hence, such details are not shown in the 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.</p>

Issue of warrants along with public issue or right issue

Warrant may be issued along with public issue or rights issue of specified securities subject to the following :

- the tenure of such warrant shall not exceed eighteen months from their date of allotment in the public/ rights issue;
- not more than one warrant shall be attached to one specified security;
- the price or conversion formula of the warrant shall be determined upfront and at least 25% of the consideration amount shall also be received upfront;
- in case the warrant holder does not exercise the option to take equity shares against any of the warrants held by this, the consideration paid in respect of such warrant shall be forfeited by the issuer.

Debarment

An issuer can not make a public issue or rights issue of specified securities 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 SEBI. If any of the promoters, directors or person 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 SEBI.

Filing of Offer Document

An issuer company can not make any public issue of securities, unless a draft offer document has been filed with SEBI through a Merchant Banker, at least 30 days prior to registering the prospectus, red herring prospectus or shelf prospectus with the Registrar of Companies (ROC) or filing the letter of offer with the designated stock exchange.

However, if SEBI specifies changes or issues observations on the draft Prospectus, such changes or comply with observation shall be made by issuer company of the lead manager within 30 days from the date of receipt of the draft Prospectus by SEBI.

SEBI may specify changes or issue observations, if any, on the draft prospectus within 30 days from the later of the date of receipt of the draft offer document or the date of receipt of satisfactory reply from the lead merchant bankers, where SEBI has sought any clarification or additional information from them or the date of receipt of clarification or information from any regulator or agency, where SEBI has sought any clarification or information from such regulator or agency or the date of receipt of a copy of in-principal approval letter issued by the recognized stock exchanges.

The lead merchant banker should while filing the offer document with SEBI, file a copy of such document with the recognized stock exchanges where the specified securities are proposed to be listed and a soft copy of the offer document should also be furnished to SEBI.

Issue of Securities in Dematerialised Form

A company can not make public or rights issue or an offer for sale of securities, unless the company enters into an agreement with a depository for dematerialisation of securities already issued or proposed to be issued to the public or existing shareholders; and the company gives an option to subscribers/ shareholders/ investors to receive the security certificates or hold securities in dematerialized form with a depository.

Security Deposit

The issuer shall deposit, before the opening of subscription list, and keep deposited with the stock exchange(s), an amount calculated at the rate of one per cent of the amount of securities offered for subscription to the public.

The amount specified shall be deposited in the manner specified by SEBI and/or stock exchange(s). The amount shall be refundable or forfeitable in the manner specified by SEBI.

Partly Paid-up Shares

These Regulations also require that all the existing partly paid-up shares must be made fully paid up or forfeited. A company can not make a public or rights issue of securities unless firm arrangements of finance through verifiable means towards 75% of the stated means of finance, excluding the amount to be raised through proposed Public/ Rights issue, have been made.

FAST TRACK ISSUES

The fast-track route of fund raising is an alternative available for companies to access public funds by way of further capital offerings. Considering the need to enable well established and compliant listed companies to access Indian primary market in a time effective manner through follow-on public offerings and rights issues, SEBI decided to enable listed companies satisfying certain specified requirements to make Fast Track Issues (FTIs). Accordingly, such listed companies are now able to proceed with follow-on public offering/rights issue by filing a copy of the Red Herring Prospectus (in case of book built issue)/Prospectus (in case of fixed price issue)

registered with the Registrar of Companies or the letter of offer filed with Designated Stock Exchange, as the case may be, with SEBI and stock exchanges. Such companies are not required to file draft offer document with SEBI and stock exchanges.

Accordingly the provisions relating to filing of offer document are not applicable to public issue of securities by a listed issuer company or a rights issue of securities by a listed issuer company, if the following conditions are satisfied:

- (a) The shares of the company have been listed on any stock exchange having nationwide terminals for a period of at least three years immediately preceding the reference date;
- (b) The “average market capitalisation of public shareholding” of the company is at least one thousand crore rupees in case of public issue and two hundred and fifty crore rupees in case of rights issue.
- (c) The annualized trading turnover of the shares of the company during six calendar months immediately preceding the month of the reference date has been at least two per cent of the weighted average number of shares listed during the said six months period;

However, for issuers whose public shareholding is less than 15% of its issued equity capital, the annualized trading turnover of its equity shares has been at least 2% of the weighted number of equity shares available as free float during such six months period.

- (d) The company has redressed at least 95% of the total shareholder/investor grievances or complaints received till the end of the quarter immediately preceding the month of the reference date;
- (e) The company has been compliance with the equity listing agreement for a period of at least three years immediately preceding the reference date;

However, 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.

Further, imposition of only monetary fines by stock exchanges on the issuer shall not be a ground for ineligibility for undertaking issuances under this regulation.

- (f) The impact of auditors’ qualifications, if any, on the audited accounts of the company in respect of the financial years for which such accounts are disclosed in the offer document does not exceed 5% of the net profit/loss after tax of the company for the respective years.
- (g) No prosecution proceedings or show cause notices issued by SEBI are pending against the company or its promoters or whole time directors as on the reference date; and
- (h) The issuer or promoter or promoter group or director of the issuer has not settled any alleged violation of securities laws through the consent or settlement mechanism with SEBI during three years immediately preceding the reference date.
- (i) The entire shareholding of the promoter group is held in dematerialised form as on the reference date.
- (j) In case of a rights issue, promoters and promoter group shall mandatorily subscribe to their rights entitlement and shall not renounce their rights, except to the extent of renunciation within the promoter group or for the purpose of complying with minimum public shareholding norms prescribed under Rule 19A of the Securities Contracts (Regulation) Rules, 1957.
- (k) The equity shares of the issuer have not been suspended from trading as a disciplinary measure during last three years immediately preceding the reference date.

- (l) The annualized delivery-based trading turnover of the equity shares during six calendar months immediately preceding the month of the reference date has been at least ten percent of the weighted average number of equity shares listed during such six months' period.
- (m) There shall be no conflict of interest between the lead merchant banker(s) and the issuer or its group or associate company in accordance with applicable regulations.

A listed issuer company satisfying all the requirements specified in this clause and filing a red herring prospectus (in case of a book built issue) or prospectus (in case of a fixed price issue) with ROC or letter of offer with Designated Stock Exchange, as the case may be, shall simultaneously with such filing or as soon thereafter as reasonably practicable, but in any case not later than the opening of the issue, file a copy thereof with SEBI.

PRICING

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

Differential Pricing

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

- (a) retail individual investors or retail individual shareholders or employees entitled for reservation making an application for a value of not more than two lakh rupees, can be offered specified securities at a price lower than the price at which net offer is made to other categories of applicants.
However, such difference shall not be more than 10% 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 should not be lower than the price offered to other applicants;
If the issuer opts for alternate method of book building, the issuer can offer specified securities to its employees at a price, lower than floor price and the difference between such price and floor price shall not be more than 10%.
- (c) in case of a composite issue, the price of the specified securities offered in the public issue can be different from the price offered in rights issue and justification for such price difference should be given in the offer document.

Price and Price Band

- (1) The issuer can 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.
However, the prospectus registered with the Registrar of Companies should contain only one price or the specific coupon rate, as the case may be.
- (2) The issuer should announce the floor price or price band at least 5 working days before the opening of the bid (in case of an initial public offer) and at least 1 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 should 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.

The announcement and the relevant financial ratios shall be disclosed on the websites of those stock exchanges where the securities are proposed to be listed and shall also be pre-filled in the application forms available on the websites of the stock exchanges.

- (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 should not be less than the face value of the specified securities. "Cap on the price band" includes cap on the coupon rate in case of convertible debt instruments.

Face Value of Equity Shares

An eligible company shall be free to make public or rights issue of equity shares in any denomination determined by it in accordance with the provisions of the Companies Act, 2013 and in compliance with the following and other norms as may be specified by SEBI from time to time.

(i) In case of initial public offer by an unlisted company:

- (a) if the issue price is ₹ 500/- or more, the issuer company shall have a discretion to fix the face value below ₹ 10/- per share subject to the condition that the face value shall in no case be less than Re. 1 per share.
- (b) if issue price is less than ₹ 500 per share, the face value shall be ₹ 10/- per share.

It may be noted that this condition is not applicable to IPO made by Government company statutory authority, or corporation or any special purpose vehicle set up by any of them which is in infrastructure sector.

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

PROMOTERS' CONTRIBUTION

Promoters' contribution in any issue shall be in accordance with the following provisions as on (i) the date of filing red herring prospectus (in case of a book built issue) or prospectus (in case of a fixed price issue) with ROC or letter of offer with Designated Stock Exchange, as the case may be, in case of a fast track issue; and (ii) the date of filing draft offer document with SEBI, in any other case.

Promoters' contribution

Unlisted Company	In case of Public Issue*	Not less than 20% of the post-issue capital
Listed Company	In case of Public Issue	To the extent of 20% of the proposed issue or 20% of the post-issue capital
Listed Company	Composite Issue**	20% of the proposed public issue or 20% of the post-issue capital.

* In case the post issue shareholding of the promoters is less than 20%, alternative investment funds may contribute for the purpose of meeting the shortfall in minimum contribution as specified for promoters, subject to a maximum of 10 % of the post issue capital.

**Rights issue component of the composite issue shall be excluded while calculating the post-issue capital.

Promoters' Contribution to be Brought in Before Public Issue Opens

Promoters shall bring in the full amount of the promoters' contribution including premium at least one day prior to the issue opening date which shall be kept in an escrow account with a Scheduled Commercial Bank and the said contribution/ amount shall be released to the company along with the public issue proceeds.

However, where the promoters' contribution has been brought prior to the public issue and has already been deployed by the company, the company shall give the cash flow statement in the offer document disclosing the use of such funds received as promoters' contribution.

If the promoters' minimum contribution exceeds ₹100 crores, the promoters shall bring in ₹100 crores before the opening of the issue and the remaining contribution shall be brought in by the promoters in advance on pro-rata basis before the calls are made on public.

Exemption from requirement of promoters' Contribution

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

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

(b) In case of 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.

(c) Rights issues

Securities ineligible for minimum promoters' contribution

(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 and alternative investment funds 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.

(c) specified securities allotted to promoters and alternative investment funds 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.

However, 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

However, Clause (b) shall not apply:

- (i) if promoters /alternative investment funds, as applicable 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 230-240 of the Companies Act, 2013, as approved by a tribunal, 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;

(2) Specified securities referred above shall be eligible for the computation of promoters' contribution, if such securities are acquired pursuant to a scheme which has been approved under sections 230-240 of the Companies Act, 2013.

LOCK-IN-REQUIREMENTS

For Securities Held by Promoters

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

- (a) The promoters contribution including contribution made by alternative investment fund is subject to lock-in-period of 3 years from the date of commencement of commercial production or date of allotment in the public issue whichever is later.
- (b) Any contribution made by promoters over and above the minimum contribution shall be subject to a lock-in-period of 1 year in case of all the companies.
- (c) In case of issue of securities by a company listed on a stock exchange for at least 3 years and having a track record of dividend payment for at least 3 immediately preceding years promoter's contribution shall not be subject to lock-in-period.

Securities Held by Persons other than Promoters

The entire pre-issue share capital, other than that locked-in as minimum promoters' contribution, shall be locked-in for a period of one year from the date of commencement of commercial production or the date of allotment in the public issue, whichever is later.

This is not applicable (i) in case of equity shares allotted to employees under employee stock option prior to initial public offer, if the issuer has made full disclosures with respect to such option and (ii) Equity shares held by a venture capital fund or alternative Investment fund of category I or a foreign venture capital investor and such equity shares shall be locked-in for a period of atleast one-year from the date of purchase by the venture capital or AIF or foreign venture capital investor.

Securities Lent to Stabilising Agent under Green Shoe Option

If the shares held by promoter(s) are lent to the Stabilizing Agent (SA) as prescribed, they should be exempted from the lock-in requirements specified above, for the period starting from the date of such lending and ending on the date on which they are returned to the same lender(s). However, the securities should be locked-in for the remaining period from the date on which they are returned to the lender.

TRANSFERABILITY OF SHARE UNDER LOCKED-IN

Shares held by promoter(s) which are locked-in, can be transferred to and amongst promoter/promoter group or to a new promoter or persons in control of the company, subject to continuation of lock-in in the hands of transferees for the remaining period and compliance of the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011, as applicable.

The securities held by persons other than promoters can be transferred to any other person holding the securities which are locked-in along with the securities proposed to be transferred, subject to the compliance of SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011. However, the lock-in on such 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 has expired.

Pledge of locked-in specified securities

Specified securities held by promoters during locked-in period are allowed to be pledged with any scheduled commercial bank or public financial institution, subject to the following:

(a) if the specified securities are locked-in in terms as prescribed in the regulation, 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 as prescribed in the regulation and the pledge of specified securities is one of the terms of sanction of the loan.

UNDERWRITING

Underwriting means an agreement with or without conditions to subscribe to the securities of a body corporate when the existing shareholders of such body corporate or the public do not subscribe to the securities offered to them.

- (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 SEBI (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.

However, atleast 75 % of the net offer to public proposed to be compulsorily allotted to qualified institutional buyers cannot be underwritten.

- (3) The issuer shall enter into underwriting agreement with the book runner, who in turn shall enter into underwriting agreement with syndicate members, indicating therein the number of specified securities which they shall subscribe to at the predetermined price in the event of under subscription in the issue.
- (4) If syndicate members fail to fulfill their underwriting obligations, the lead book runner shall fulfill the underwriting obligations.
- (5) The book runners and syndicate members shall not subscribe to the issue in any manner except for fulfilling their underwriting obligations.
- (6) In case of every underwritten issue, the lead merchant banker or the lead book runner shall undertake minimum underwriting obligations as specified in the SEBI (Merchant Bankers) Regulations, 1992.
- (7) Where 100% of the offer through offer document is underwritten, the underwriting obligations shall be for the entire 100% of the offer through offer document and shall not be restricted upto the minimum subscription level.

In respect of an underwritten issue, the lead merchant banker shall ensure that the relevant details of underwriters are included in the offer document as follows:

Underwriting of the issue:

- (a) Names and addresses of the underwriters and the amount underwritten by them
- (b) Declaration by board of directors of the issuer company that the underwriters have sufficient resources to discharge their respective obligations.”

In case of under subscription at an issue, the Lead Merchant Banker responsible for underwriting arrangements shall invoke underwriting obligations and ensure that the underwriters pay the amount of development and the same shall be incorporated in the inter-se allocation of responsibilities accompanying the due diligence certificate submitted by the Lead Merchant Banker to SEBI.

Manner of Call

If the issuer proposes to receive subscription monies in calls, it shall ensure that the outstanding subscription money is called within 12 months from the date of allotment in the issue and if any applicant fails to pay the call money within the said 12 months, the equity shares on which there are calls in arrear along with the subscription money already paid on such shares shall be forfeited.

However, it shall not be necessary to call the outstanding subscription money within 12 months, if the issuer has appointed a monitoring agency.

Despatch of Issue Material

The lead merchant banker must ensure that for public issues offer documents and other issue materials including forms for ASBA are dispatched to the designated stock exchanges, syndicate members registrar to issue and share transfer agents, depository participants, stock brokers, underwriters, bankers to the issue, investors associations, self certified syndicate banks, etc. in advance as agreed upon. In the case of rights issues also, lead merchant banker must ensure that the abridged letters of offer along with composite application form are dispatched through registered post or speed post to all shareholders at least 3 days before the date of opening of the issue. Where a specific request for letter of offer is received from any shareholder, the lead Merchant Banker shall ensure that the letter of offer is made available to such shareholder.

ISSUE OPENING DATE

Subject to the compliance with Section 26 of the Companies Act, 2013 a public issue may be open within 12 months from the date of issuance of the observation letter by SEBI, if any, or within 3 months of expiry from 31st day from the date of filing of draft offer document with SEBI, if no observation letter is issued. However, in case of a fast track issue, the issue must open within the period stipulated in Section 26(1)(a) of the Companies Act, 2013 and rules made thereunder.

In case of shelf prospectus, the first issue can be opened within 3 months of issuance of observations by SEBI.

PERIOD OF SUBSCRIPTION

A public issue must be kept open for atleast 3 working days but not more than 10 working days including the days for which the issue is kept open in case of revision in price band. 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 should be extended for a minimum period of 3 working days. However, the total bidding period should not exceed 10 working days. Rights issue should be kept open for a minimum period of 15 days and for a maximum period of 30 days.

MINIMUM NUMBER OF SHARE APPLICATIONS AND APPLICATION MONEY

The minimum application value shall be within the range of ₹ 10,000 to ₹ 15,000. The issuer company, in consultation with the merchant banker, shall stipulate the minimum application size (in terms of number of specified securities) falling within the aforesaid range of minimum application value and make upfront disclosures in this regard, in the offer document.

Thus, the 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.

Assuming an issue is being made at a price of ₹ 900 per equity share. In this case, the issuer in consultation with the lead merchant banker can determine the minimum application lot within the range of 12 – 16 equity shares (in value terms between ₹10,000- ₹15,000), as explained hereunder:

<i>Options</i>	<i>I</i>	<i>II</i>	<i>III</i>	<i>IV</i>	<i>V</i>
Lot Size @ ₹ 900/- per share	12 shares	13 shares	14 shares	15 shares	16 shares
Application / Bid amount for 1 lots	10800	11700	12600	13500	14400
Application / Bid amount for 2 lots	21600	23400	25200	27000	28800
Application / Bid amount for 4 lots	43200	46800	50400	50400	57600
Application / Bid amount for 8 lots	86400	93600	100800	108000	115200
Application / Bid amount for 16 lots	172800	187200	–	–	–
Application / Bid amount for 18 lots	194400	–	–	–	–

Applications can be made in multiples of the minimum size /value so stipulated in the offer document by the issuer and merchant banker within the range of ₹ 5000-7000.

The minimum application moneys to be paid by an applicant along with the application money shall not be less than 25% of the issue price.

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

ISSUE OF ADVERTISEMENTS

Advertisement includes notices, brochures, pamphlets, circulars show cards, catalogues, hoardings, placards, posters, insertion in newspapers, pictures, films, cover pages of offer documents or any other print medium radio, television programmes through any electronic medium.

Pre-issue advertisement

The issuer company shall soon after receiving final observations, if any, on the offer document from SEBI, make an advertisement in an English National daily with wide circulation, one Hindi National newspaper and a regional language newspaper with wide circulation at the place where the registered office of the issuer is situated, in the prescribed format, subject to section 30 of the Companies Act, 2013.

Post-issue Advertisements

The post-issue Merchant Banker is required to ensure that in all issues, advertisement giving details relating to oversubscription, basis of allotment, number, value and percentage of applications, including ASBA number, value and percentage of successful allottees for all application including ASBA, date of completion of despatch of refund orders or instructions to Self Certified Syndicate Banks by the Registrar, date of completion of despatch of refund orders or instructions to Self Certified syndicate banks by the registrar, date of despatch of certificates and date of filing of listing application is released within 10 days from the date of completion of the various activities at least in an English National Daily with wide circulation, one Hindi National Paper and a Regional language daily circulated at the place where registered office of the issuer company is situated. Post-issue Lead Merchant Banker is required to ensure that issuer company/advisors/brokers or any other entity connected with the issue do not publish any advertisement stating that the issue has been oversubscribed or indicating investors' response to the issue, during the period when the public issue is still open for subscription by the public.

MANDATORY COLLECTION CENTRES

The Regulations require a minimum number of collection centres for an issue of capital to be at the four metropolitan centre viz. Mumbai, Delhi, Kolkata and Chennai and at all such centres where the stock exchanges are located in the region in which the registered office of the company is situated. In addition, all designated branches of Self Certified Syndicate Banks, as displayed on the websites of such banks and of SEBI, shall be deemed to be mandatory collection centres. However, the issuer company is free to appoint as many collection centres as it may deem fit in addition to the above minimum requirement.

MINIMUM SUBSCRIPTION

The minimum subscription to be received in an issue should not be less than ninety percent of the offer through offer document. However, in the case of an initial public offer, the minimum subscription to be received shall be subject to allotment of minimum number of specified securities, as prescribed in sub-clause (b) of clause (2) of rule 19 of Securities Contracts (Regulation) Rules, 1957.

In the event of non receipt of minimum subscription, all applications moneys received should 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.
- (b) seventy days of the closure of the issue, in case of an underwritten issue where minimum subscription

including devolvement obligations paid by the underwriters is not received within 60 days of the closure of issue.

The requirement of minimum subscription is not applicable to offer for sale.

For Non-underwritten issues

(a) If the issuing company does not receive the minimum subscription of ninety per cent of the offer through offer document on the date of closure of the issue, or if the subscription level falls below ninety per cent after the closure of issue on account of cheques having being returned unpaid or withdrawal of applications, the issuing company shall forthwith refund the entire subscription amount received.

(b) If the issuing company fails to refund the entire subscription amount within fifteen days from the date of the closure of the issue, it is liable to pay the amount with interest to the subscribers at the rate of fifteen per cent per annum for the period of delay.

For underwritten issues

If the issuing company does not receive the minimum subscription of ninety per cent of the offer through offer document including devolvement of underwriters within sixty days from the date of closure of the issue, the issuing company shall forthwith refund the entire subscription amount received with interest to the subscribers at the rate of fifteen per cent per annum for the period of delay beyond sixty days.

RESTRICTION ON FURTHER CAPITAL ISSUES

Issuer shall not make any further issue of specified securities in any manner whether by way of Public issue, Rights issue, Preferential issue, Qualified institutions placement, Issue of bonus shares or otherwise:-

(a) in case of a fast track issue, during the period between the date of registering the red herring prospectus (in case of a book built issue)

or

prospectus (in case of a fixed price issue) with the ROC 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

(b) in case of other issues, during the period between the date of filing of draft offer document with SEBI 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.

PROPORTIONATE ALLOTMENT

The allotment to applicants other than retail individual investor and anchor investor shall be on a proportionate basis within the specified categories rounded off to the nearest integer subject to a minimum allotment being equal to the minimum application size as fixed and disclosed by the issuer.

The allotment of specified securities to each retail individual investor shall not be less than the minimum bid lot, subject to availability of shares in retail individual investor category, and the remaining available shares, if any, shall be allotted on a proportionate basis.

BASIS OF ALLOTMENT

In a public issue of securities, the Executive Director/Managing Director of the Designated Stock Exchange along with the post issue Lead Merchant Banker and the Registrars to the Issue shall be responsible to ensure that the basis of allotment is finalised in a fair and proper manner in accordance with this regulations. However, in case of book building portion of a book built public issue, SEBI (ICDR) Regulations, 2009 shall be applicable.

The listed company would ensure that all steps for completion of the necessary formalities for listing and commencement of trading at all stock exchanges where the securities are to be listed have been taken within 7 working days of finalisation of basis of allotment.

COORDINATION WITH INTERMEDIARIES

The Post-issue lead merchant banker shall maintain close co-ordination with the Registrars to the Issue and arrange to depute its officers to the offices of various intermediaries at regular intervals after the closure of the issue to monitor the flow of applications from collecting bank branches, and/or self certified syndicate banks processing of the applications including application form for applications supported by blocked amount and other matters till the basis of allotment is finalised, despatch of security certificates and refund orders are completed and securities are listed.

Any act of omission or commission on the part of any of the intermediaries noticed during such visits shall be duly reported to SEBI.

In case there is a devolvement on underwriters, the merchant banker is required to ensure that the notice for devolvement containing the obligation of the issuer is issued within a period of 10 days from the date of closure of the issue.

In case of undersubscribed issues, the merchant bank is required to furnish information in respect of underwriters who have failed to meet their underwriting devolvement to SEBI in the format specified in these regulations.

The post-issue merchant banker is required to confirm to the bankers to the issue by way of copies of listing and trading approval that all formalities in connection with the issue have been completed and that the banker is free to release the money to the issuer or refund it in case of failure of the issue.

MINIMUM OFFER TO PUBLIC

The minimum net offer to the public shall be subject to the provision of clause (b) of sub-rule (2) of rule 19 of Securities Contracts (Regulations) Rules, 1957

RESERVATION ON COMPETITIVE BASIS

Reservation on competitive basis means reservation wherein specified securities are allotted in portion 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.

According to SEBI (ICDR) Regulations, 2009, there are certain persons eligible for reservation on competitive basis.

(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, in case of 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:

However, 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 SEBI, are associated with the issuer as depositors, bondholders or subscribers to services of the issuer making an initial public offer. However, 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 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:

However, 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 5% of the post issue capital of the issuer;
- (b) reservation for shareholders shall not exceed 10% of the issue size;
- (c) reservation for persons who as on the date of filing the draft offer document with SEBI have business association as depositors, bondholders and subscribers to services with the issuer making an initial public offer shall not exceed 5% 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) value of allotment to any employee made shall not exceed two lakh rupees.

However, in the event of under-subscription in the employee reservation portion, the unsubscribed portion may be allotted on a proportionate basis, for a value in excess of two lakhs rupees, subject to the total allotment to an employee not exceeding five lakhs rupees.

(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.

ALLOCATION IN NET OFFER TO PUBLIC

A person shall not 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.

Note: -

In case of an issue made through the book building process as per regulation 26(1), then the allocation in the net offer to public category shall be as follows:

- not less than 35 % to retail individual investors;
- not less than 15 % to non-institutional investors;
- not more than 50% to qualified institutional buyers, 5 % of which shall be allocated to mutual fund

In case of an issue made through the book building process under regulation 26(2), the allocation in the net offer to public category shall be as follows:

- not more than 10% to retail individual investors;
- not more than 15% to non-institutional investors;
- not less than 75% to qualified institutional buyers, 5% of which shall be allocated to mutual fund

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

- Minimum 50% to retail individual investors; and
- Remaining to:
 - (i) individual applicants other than RII and
 - (ii) other investors including corporate bodies or institutions, irrespective of the number of specified securities applied for;
- The unsubscribed portion in either of the categories specified above may be allocated to applicants in the other category.

1. In case of an issue made through Book Building process under regulation 26(1) and 26(2), addition of 5% allocation available to mutual funds shall be eligible for allocation under the balance available for qualified institutional buyers.
2. The issuer may allocate up to 60% of the portion available for allocation to qualified institutional buyers to an anchor investor.
3. For above purpose, if the retail individual investor category is entitled to more than 50% on proportionate basis, the retail individual investors shall be allocated that higher percentage.

Offer Document to be Made Public

The draft offer document filed with SEBI shall be made public for comments, if any, for a period of 21 days from the date of filing the offer document with SEBI by hosting it on the websites of the SEBI, recognized stock exchanges where specified securities are proposed to be listed and merchant bankers associated with the issue.

After a period of 21 days from the date the draft offer document was made public, the Lead Merchant Bankers shall file with SEBI a statement giving information of the comments received by them or issuer during that period and the consequential changes, if any, to be made in the draft offer document.

Due Diligence

A merchant banker holding a valid certificate of registration is required to be appointed to manage the issue. A Memorandum of Understanding (MOU) is required to be entered into between lead merchant bankers and the issuer company specifying their mutual rights, liabilities and obligations relating to the issue.

MOUs should not contain any clauses contrary to the provision of the Companies Act, 2013 and SEBI (Merchant Bankers) Rules and Regulations, 1992 so as to diminish the liabilities and obligations of the lead merchant banker or the issuer company. Lead manager is required to exercise due diligence. The standard of due diligence shall be such that merchant banker shall satisfy himself about all aspects of offering, veracity and adequacy of disclosure in offer document. Lead manager who is responsible for preparation of the offer documents is required to submit to SEBI draft prospectus complete in all respects alongwith the Due Diligence Certificate, *Inter se* allocation of Responsibilities Certificate and a copy of Memorandum of Understanding and the requisite fee in accordance with SEBI (Merchant Bankers) Rules and Regulations, 1992.

In addition, due diligence certificate to be furnished alongwith the draft prospectus, lead managers are also

required to –

- (i) Certify that all the amendments suggested/observations made by SEBI have been given effect to in the prospectus;
- (ii) Furnish a fresh due diligence certificate at the time of filing the prospectus with the Registrar of Companies;
- (iii) Furnish a fresh certificate immediately before the opening of the issue that no corrective action is needed; and
- (iv) Furnish a fresh and final compliance certificate before the issue is closed for subscription.

Allotment of Securities

The company agrees that as far as possible allotment of securities offered to the public shall be made within 15 days of the closure of public issue. The company further agrees that it shall pay interest @15% per annum if the allotment letters/ refund orders have not been despatched to the applicants or if, in a case where the refund or portion thereof is made in electronic manner, the refund instructions have not been given to the clearing system in the disclosed manner within 15 days from the date of the closure of the issue. In case of book-built issue the refund instruction have not been given to the clearing system in the disclosed manner within 15 days from the date of the closure of the issue. However, applications received after the closure of issue in fulfillment of underwriting obligations to meet the minimum subscription requirement, shall not be entitled for the said interest.

Despatch of Letter of Allotment and Share Certificates

The Company shall take such steps as are necessary to ensure the completion of allotment and despatch of letters of allotment and refund orders to the applicants including NRIs soon after the basis of allotment has been approved by the stock exchanges and in any case not later than the statutory time limit and in the event of failure to do so pay interest to the applicants as provided under the Companies Act, 2013 and the rules made thereunder.

Compliance Officer

Every company making a public issue is required to appoint a compliance officer and intimate the name of the compliance officer to SEBI. Compliance Officer shall directly liaise with SEBI with regard to compliance with various laws, rules, regulations, and other directives issued by SEBI and investor complaints related matters. He is also required to co-ordinate with regulatory authorities in various matters and provide necessary guidance so as to ensure compliance internally and ensure that observations made/deficiency pointed out by SEBI do not recur. As per Regulation 6(1) of the SEBI (LODR) Regulations, 2015 the Company Secretary shall be the Compliance Officer of the Company, who shall be responsible for ensuring the correctness, authenticity and comprehensiveness of the information, statements, reports etc. filled under corporate filing and dissemination system as specified in the listing agreement.

Redressal of Investors Grievances

These regulations make it necessary for companies to assign high priority to investor grievances and ensure that all preventive steps have been taken to minimise the number of complaints. Proper grievance monitoring and redressal system should be set in consultation with the lead merchant banker and Registrar to an issue and necessary measures to resolve the grievances quickly and lead merchant banker should closely associate with the post issue refund and allotment activities and regularly monitor investor grievances arising therefrom.

The offer documents shall necessarily disclose the arrangements or any mechanism evolved by the company for redressal of investor grievances.

1. The company shall disclose the time normally taken by it for disposal of various types of investor grievances.
2. Similar disclosure shall be made in regard to the listed companies under the same management for the period of 3 years prior to the date of filing of the offer documents with ROC/Stock Exchange.

Powers of SEBI

SEBI may either suo motu or on receipt of information or on completion or pendency of any inspection, inquiry or investigation, in the interests of investors or the securities market, issue such directions or orders as it deems fit including any or all of the following:

(a) directing the persons concerned not to access the securities market for a specified period.

(b) directing the person concerned to sell or divest the securities.

(a) directing the persons concerned not to access the securities market for a specified period.

However, SEBI shall, either before or after issuing such direction or order, give a reasonable opportunity of being heard to the person concerned.

Further that if any interim direction or order is required to be issued, SEBI may give post-decisional hearing to the person concerned.

SEBI have power to remove any difficulties in the application or interpretation of these regulations, SEBI may relax the strict enforcement of any requirement of these regulations or issue clarifications through guidance notes or circulars after recording reasons in writing.

Chapter XI of SEBI ICDR Regulations empowers SEBI to issue directions to the persons concerned, the stock exchanges and the intermediaries.

In case of the violation of these regulations, SEBI has been empowered to direct the persons concerned to refund any money collected under an issue to the investors with or without requisite interest as the case may be and not to access the capital market for a particular period. In respect of violations by stock exchanges, SEBI can direct the exchange concerned not to list or permit trading in the securities and to forfeit the security deposit by the issuer company. In case of violations by intermediaries, SEBI may suspend or cancel the certificate of registration of any intermediary who fails to exercise due diligence or fails to comply with the obligations entrusted under the guidelines or who is alleged to have updated any of these guidelines. SEBI is under an obligation to follow the specified procedures provided under the regulations dealing with such intermediaries.

Disclaimer Clause of SEBI

SEBI notified the format of issue advertisement in Schedule XIII of SEBI (ICDR) Regulations. This provide for inclusion of SEBI Disclaimer Clause which reads as under:

“Disclaimer Clause of SEBI – SEBI only gives its observations on the offer documents and this does not constitute approval of either the issue or the offer document.”

BOOK BUILDING

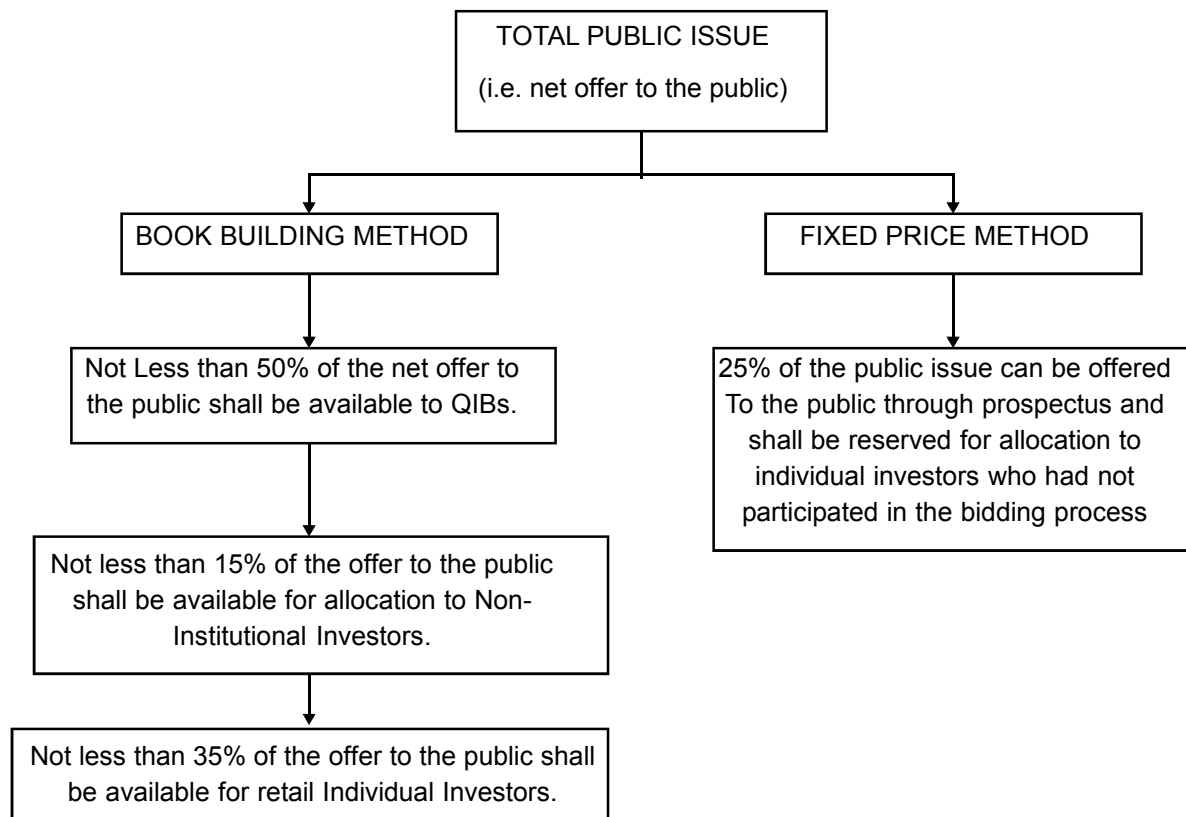
Book Building means a process undertaken to elicit demand and to assess the price for determination of the quantum or value of specified securities or Indian Depository Receipts, as the case may be.

The book building process in India is very transparent. All investors including small investors can see on an hourly basis where the book is being built before applying. According to this method, share prices are determined on the basis of real demand for the shares at various price levels in the market.

DIFFERENCE BETWEEN FIXED PRICE PROCESS AND BOOK BUILDING PROCESS

Features	Fixed Price process	Book Building process
Pricing	Price at which the securities are offered /allotted is known in advance to the investor.	Price at which securities will be offered/allotted is not known in advance to the investor. Only an indicative price range is known.
Demand	Demand for the securities offered is known only after the closure of the issue.	Demand for the securities offered can be known everyday as the book is built.
Payment	Payment if made at the time of subscription wherein refund is given after allocation.	Payment only after allocation

OFFER TO PUBLIC THROUGH BOOK BUILDING PROCESS



1. An issuer company may, subject to the requirements specified make an issue of securities to the public through a prospectus through 100% of the net offer to the public through book building process.
2. Reservation to the extent of percentage specified in these Regulations can be made only to the following categories:
 - (a) employees and in case of a new issuer, persons who are in permanent and full time employment of the promoting companies excluding the promoter and the relative of promoter of such companies.
 - (b) 'shareholders of the listed promoting companies in the case of a new company and shareholders of listed group companies in the case of an existing company' on a 'competitive basis' or on a 'firm allotment basis' excluding promoters. However, if the promoting companies are designated financial institutions or state or central financial institutions, the shareholder of such promoting companies shall be excluded for this purpose.
 - (c) persons who, on the date of filing of the draft offer document with SEBI, have business association, as depositors, bondholders and subscribers to services, with the issuer making an initial public offering.

However, no reservation can be made for the issue management team, syndicate members, their promoters, directors and employees and for the group/associate companies of issue management team and syndicate members and their promoters, directors and employees.

3. The issuer company is required to enter into an agreement with one or more of the Stock Exchange(s) which have the requisite system of on-line offer of securities. The agreement would cover *inter-alia*, the rights, duties, responsibilities and obligations of the company and stock exchange (s) *inter se*. The agreement may also provide for a dispute resolution mechanism between the company and the stock exchange.

The company may also apply for listing of its securities on an exchange other than the exchange through which it offers its securities to public through the on-line system.

4. The Lead Merchant Banker shall act as the Lead Book Runner. In case the issuer company appoints more than one merchant banker, the names of all such merchant bankers who have submitted the due diligence certificate to SEBI, may be mentioned on the front cover page of the prospectus. A disclosure to the effect that "the investors may contact any of such merchant bankers, for any complaint pertaining to the issue" is required to be made in the prospectus, after the "risk factors".
5. The lead book runner/issuer may designate, in any manner, the other Merchant Bankers if the inter-se allocation of responsibilities amongst the merchant bankers is disclosed in the prospectus on the page giving the details of the issue management team and a co-ordinator has been appointed amongst the lead book runners, for the purpose of co-ordination with SEBI. However, the names of only those merchant bankers who have signed the inter-se allocation of responsibilities would be mentioned in the offer document on the page where the details of the issue management team is given.
6. The primary responsibility of building the book is of the Lead Book Runner. The Book Runner(s) may appoint those intermediaries who are registered with SEBI and who are permitted to carry on activity as an 'Underwriter' as syndicate members. The Book Runner(s)/syndicate members shall appoint brokers of the exchange, who are registered with SEBI, for the purpose of accepting bids, applications and placing orders with the company and ensure that the brokers so appointed are financially capable of honouring their commitments arising out of defaults of their clients/investors, if any. However, in case of application supported by blocked amount, Self Certified Syndicate Banks, Registrar to Issue and Share Transfer Agents, Depository Participants shall accept and upload the details of such application in electronic bidding system of the stock exchange.
7. The brokers, and Self Certified Syndicate Banks, Registrar to Issue and Share Transfer Agents, Depository Participants accepting applications and application monies, are considered as 'bidding/collection centres'. The broker/s so appointed, shall collect the money from his/their client for every order placed by him/them and in case the client/investors fails to pay for shares allocated as per the Guidelines, the broker shall pay such amount.
8. In case of Applications Supported by Blocked Amount (ASBA), the Self Certified Syndicate Banks shall follow the procedure specified by SEBI in this regard. The company shall pay to the SEBI registered

intermediaries a commission/fee for the services rendered by him/them. The exchange shall ensure that the broker does not levy a service fee on his clients/investors in lieu of his services.

The draft prospectus containing all the disclosures except that of price and the number of securities to be offered to the public shall be filed by the Lead Merchant Banker with SEBI. The total size of the issue shall be mentioned in the draft prospectus.

9. The red herring prospectus shall disclose, either the floor price of the securities offered through it or a price band along with the range within which the price can move, if any.

However, the issuer may not disclose the floor price or price band in the red herring prospectus if the same is disclosed in case of an initial public offer, at least two working days before the opening of the bid and in case of a further public offer, at least one working day before the opening of the bid, by way of an announcement in all the newspapers in which the pre-issue advertisement was released by the issuer or the merchant banker;

Further, the announcement shall contain the 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 offer document.

Where the issuer opts not to make the disclosure of the price band or floor price in the red-herring prospectus in terms of the foregoing proviso, the following shall be additionally disclosed in the red-herring prospectus:

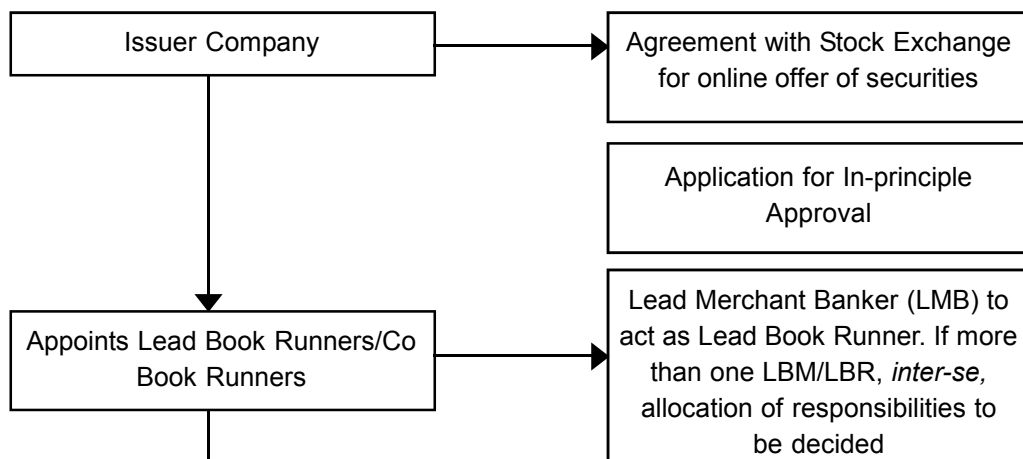
- (a) a statement that the floor price or price band, as the case may be, shall be disclosed atleast two working days (in case of an initial public offer) and atleast one working day (in case of a further public offer) before the opening of the bid;
- (b) a statement that the investors may be guided in the meantime by the secondary market prices in case of public offer;
- (c) names and editions of the newspapers where the announcement of the floor price or price band would be made;
- (d) names of websites (with address), journals or other media in which the said announcement will be made.

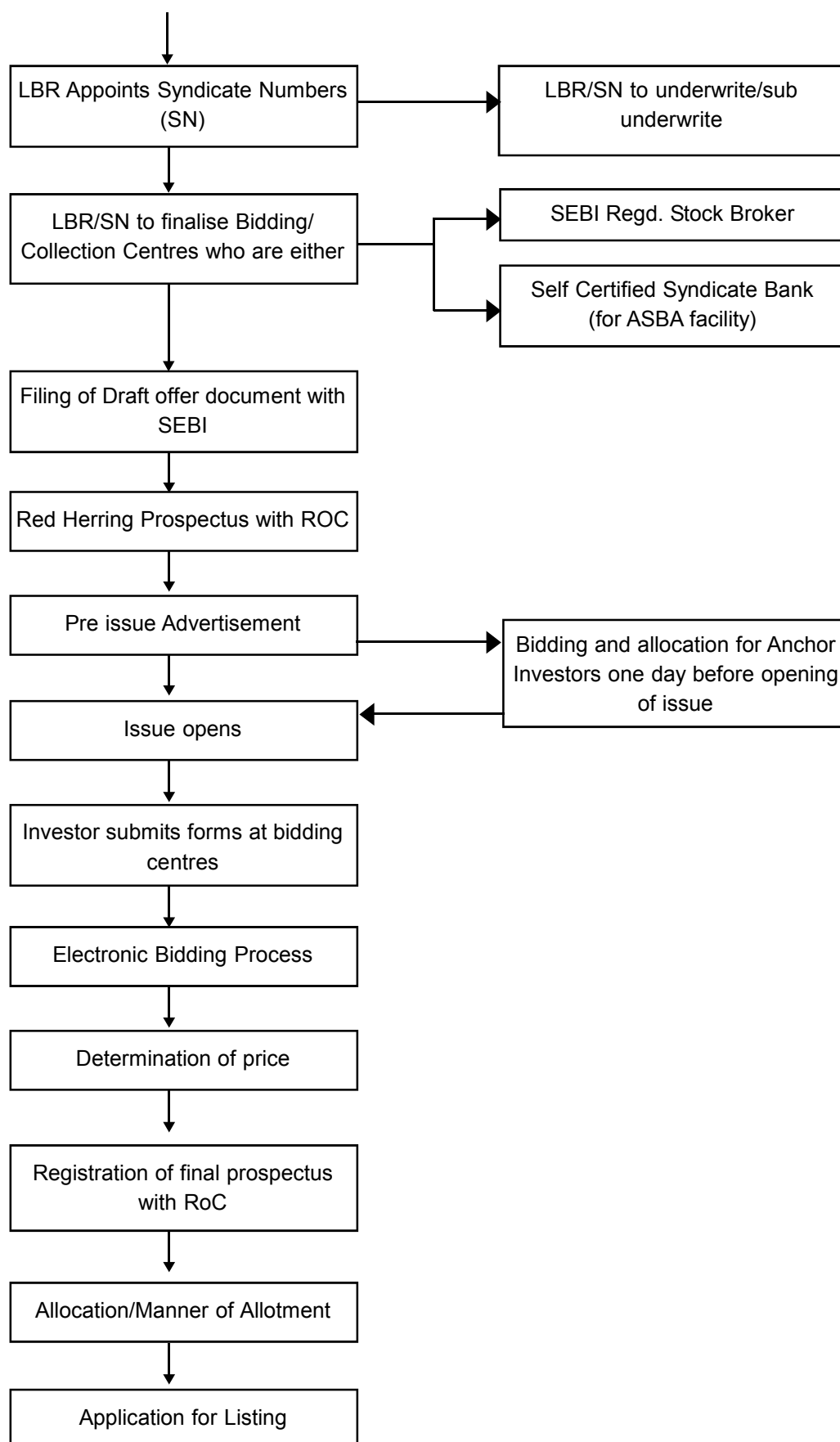
Where the issuer decides to opts for price band instead of floor price, the lead book runner shall ensure compliance with the following conditions:

- (a) The cap of the price band should not be more than 20% of the floor of the band; i.e., cap of the price band shall be less than or equal to 120% of the floor of the price band.
 - (b) The price band can be revised during the bidding period in which case the maximum revision on either side shall not exceed 20% i.e floor of price band can move up or down to the extent of 20% of floor of the price band disclosed in the red herring prospectus and the cap of the revised price band will be fixed in accordance with Clause (a) above;
 - (c) Any revision in the price band shall be widely disseminated by informing the stock exchanges, by issuing press release and also indicating the change on the relevant website and the terminals of the syndicate members.
 - (d) In case the price band is revised, the bidding period shall be extended for a further period of three days, subject to the total bidding period not exceeding ten working days.
 - (e) The manner in which the shortfall, if any, in the project financing, arising on account of lowering of price band to the extent of 20% will be met shall be disclosed in the red herring prospectus. It shall also be disclosed that the allotment shall not be made unless the financing is tied up.
10. In case of appointment of more than one Lead Merchant Banker or Book Runner for book building, the rights, obligations and responsibilities of each should be delineated. In case of an under subscription in an issue, the shortfall shall have to be made good by the Book Runner(s) to the issue and the same shall be incorporated in the *inter se* allocation of responsibility as provided in the Regulations.

11. The issuer company shall circulate the application forms to the Brokers.
12. The pre-issue obligations and disclosure requirements shall be applicable to issue of securities through book building unless stated otherwise in these regulations.
13. The Book Runner(s) and the issuer company shall determine the issue price based on the bids received through the 'syndicate members' and 'self certified syndicate banks'.
14. Retail individual investors may bid at "cut off" price instead of their writing the specific bid prices in the bid forms.
15. On determination of the price, the number of securities to be offered shall be determined i.e. issue size divided by the price which has been determined.
16. Once the final price (cut-off price) is determined all those bidders whose bids have been found to be successful shall become entitle for allotment of securities.
17. No incentive, whether in cash or kind, shall be paid to the investors who have become entitled for allotment of securities.
18. The broker may collect an amount to the extent of 100% of the application money as margin money from the clients/investors before he places an order on their behalf. The margin collected shall be uniform across all categories of investors.
19. Bids for securities beyond the investment limit prescribed under relevant laws shall not be accepted by the syndicate members/brokers from any category of clients/investors.
20. The lead book runner may reject a bid placed by a qualified institutional buyer for reasons to be recorded in writing provided that such rejection shall be made at the time of acceptance of the bid and the reasons therefor shall be disclosed to the bidders. Necessary disclosures in this regard shall also be made in the offer document.
21. On determination of the entitlement, the information regarding the same i.e. the number of securities which the investor becomes entitled shall be intimated immediately to the investors.
22. The final prospectus containing all disclosures as per these Guidelines including the price and the number of securities proposed to be issued shall be filed with the Registrar of Companies.
23. Arrangement shall be made by the issuer for collection of the applications by appointing mandatory collection centres as per these Regulations.
24. The bidding terminals shall contain a online graphical display of demand and bid prices updated at periodic intervals not exceeding 30 minutes. The book running lead manager shall ensure the availability of adequate infrastructure with syndicate members for data entry of the bids in a timely manner.
25. The investors who had not participated in the bidding process or have not received intimation of entitlement of securities may also make an application.

BOOK BUILDING PROCESS THROUGH A FLOWCHART





ADDITIONAL DISCLOSURES IN CASE OF BOOK BUILDING

Apart from meeting the disclosure requirements as specified in these regulations, the following disclosures shall be suitably made:

- (i) The particulars of syndicate members, brokers, self certified syndicate banks, registrars, bankers to an issue, etc.
- (ii) The following statement shall be given under the 'basis for issue price':
 "The issue price has been determined by the Issuer in consultation with the Book Runner(s), on the basis of assessment of market demand for the offered securities by way of Book-building."
- (iii) The following accounting ratios shall be given under the basis for issue price for each of the accounting periods for which the financial information is given:
 1. EPS, pre-issue, for the last three years (as adjusted for changes in capital).
 2. P/E pre-issue
 3. Average return on net-worth in the last three years.
 4. Net-Asset value per share based on last balance sheet.
 5. Comparison of all the accounting ratios of the issuer company as mentioned above with the industry average and with the accounting ratios of the peer group (i.e companies of comparable size in the same industry. (Indicate the source from which industry average and accounting ratios of the peer group has been taken)
 6. The accounting ratios disclosed in the offer document shall be calculated after giving effect to the consequent increase of capital on account of compulsory conversions outstanding, as well as on the assumption that the options outstanding, if any, to subscribe for additional capital shall be exercised)
- (iv) The proposed manner of allocation among respective categories of investors, in the event of under subscription.

Procedure for Bidding

The process of bidding should be in compliance of the following requirements:

- (a) Bidding process shall be only through an electronically linked transparent bidding facility provided by recognised stock exchange(s).
- (b) The lead book runner shall ensure the availability of adequate infrastructure with syndicate members for data entry of the bids in a timely manner.
- (c) The syndicate members shall be present at the bidding centres so that at least one electronically linked computer terminal at all the bidding centres is available for the purpose of bidding.
- (d) During the period, when the issue is open to the public for bidding, the applicants may approach the stock brokers of the stock exchange/s through which the securities are offered under on-line system or Self Certified Syndicate Banks, Registrar to Issue and Share Transfer Agents, Depository Participants, as the case may be, to place an order for bidding for the specified securities.
- (e) Every stock broker shall accept orders from all clients/investors who place orders through him and every Self Certified Syndicate Bank, Registrar to Issue and Share Transfer Agents, Depository Participants shall accept Applications Supported by Blocked Amount from ASBA investors.
- (f) Applicants who are qualified institutional buyers shall place their bids only through the stock brokers who shall have the right to verify the bids;

- (g) The bidding terminals shall contain an online graphical display of demand and bid prices updated at periodic intervals, not exceeding thirty minutes.
- (h) At the end of each day of the bidding period, the demand including allocation made to anchor investors, shall be shown graphically on the bidding terminals of syndicate members and websites of recognised stock exchanges offering electronically linked transparent bidding facility, for information of public.
- (i) The retail individual investors may either withdraw or revise their bids until closure of the Issue.
- (j) The issuer may decide to close the bidding by qualified institutional buyers one day prior to the closure of the issue subject to the following conditions:
 - (i) bidding shall be kept open for a minimum of three days for all categories of applicants;
 - (ii) disclosures are made in the red herring prospectus regarding the issuer's decision to close the bidding by qualified institutional buyers one day prior to closure of issue.
- (k) The qualified institutional buyers and the non-institutional investors shall neither withdraw nor lower the size of their bids at any stage .
- (l) The identity of qualified institutional buyers making the bidding shall not be made public.
- (m) The stock exchanges shall continue to display on their website, the data pertaining to book built issues in an uniform format, *inter alia* giving category-wise details of bids received, for a period of at least three days after closure of bids.

Alternate Method of Book Building

In case of further public offers, the issuer may opt for an alternate method of book building, subject to the following:

- (a) Issuer shall follow the procedure laid down in Part A of Schedule XI of SEBI (ICDR) Regulations, 2009.
- (b) The issuer may mention the floor price in the red herring prospectus or if the floor price is not mentioned in the red herring prospectus, the issuer shall announce the floor price at least one working day before opening of the bid in all the newspapers in which the pre-issue advertisement was released.
- (c) Qualified institutional buyers shall bid at any price above the floor price.
- (d) The bidder who bids at the highest price shall be allotted the number of securities that he has bided for and then the bidder who has bided at the second highest price and so on, until all the specified securities on offer are exhausted.
- (e) Allotment shall be on price priority basis for qualified institutional buyers.
- (f) Allotment to non-institutional investors and employees of the issuer shall be made proportionately .
- (g) Where, however the number of specified securities bided for at a price is more than available quantity, then the allotment shall be done on proportionate basis.
- (h) Retail individual investors, non-institutional investors and employees shall be allotted specified securities at the floor price.
- (i) The issuer may:-
 - (A) place a cap either in terms of number of specified securities or percentage of issued capital of the issuer that may be allotted to a single bidder;
 - (B) decide whether a bidder be allowed to revise the bid upwards or downwards in terms of price and/or quantity;
 - (C) decide whether a bidder be allowed single or multiple bids.

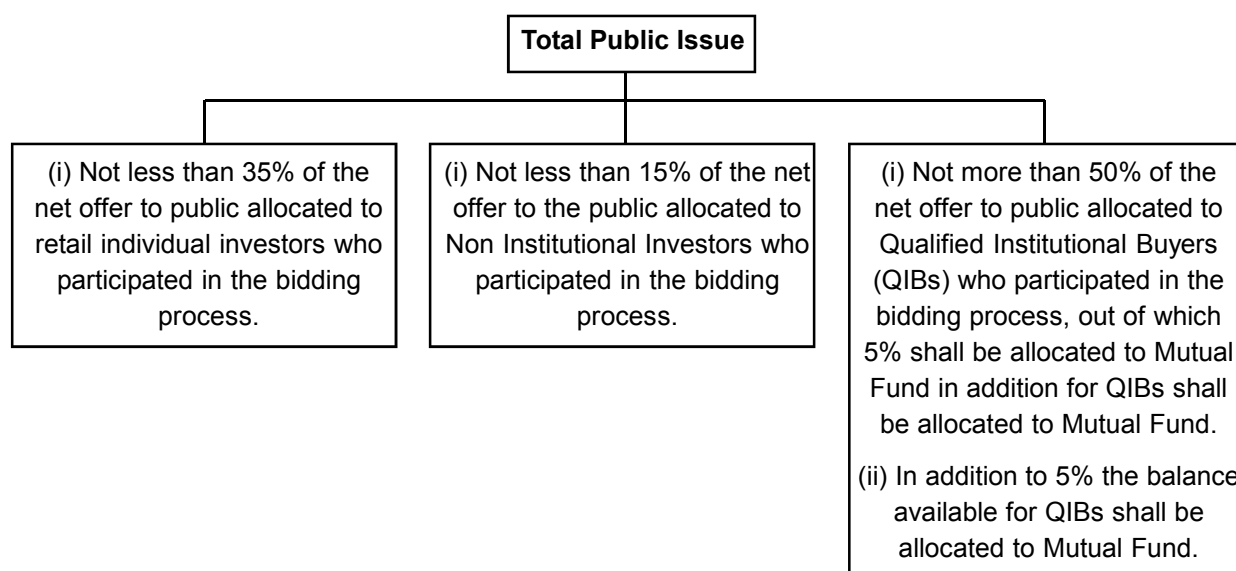
MAINTENANCE OF BOOKS AND RECORDS

A final book of demand showing the result of the allocation process shall be maintained by the book runner/s. The Book Runner/s and other intermediaries in the book building process associated shall maintain records of the book building prices. SEBI has the right to inspect the records, books and documents relating to the Book building process and such person shall extend full cooperation.

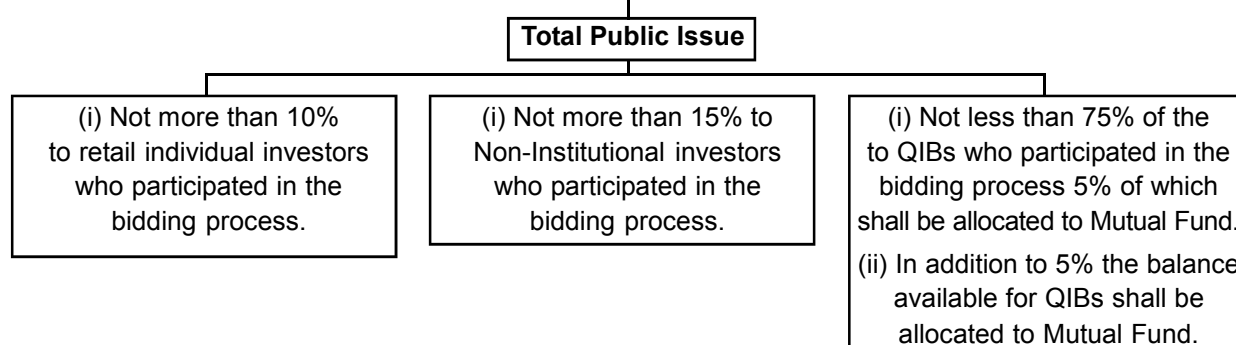
All references mentioned above with respect to draft prospectus shall be construed as having been made to 'red herring prospectus' in application to fast track issues.

ALLOCATION/ALLOTMENT PROCEDURE

100% of the Net offer to the public through 100% book building process



In case of Alternative Eligibility Norms



ANCHOR INVESTORS

"Anchor investor" means a qualified institutional buyer 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:

(a) Allocation to Anchor Investors shall be on a discretionary basis and subject to the following:

- (i) Maximum of 2 such investors shall be permitted for allocation upto ₹ 10 crore;
- (ii) Minimum of 2 and maximum of 15 such investors shall be permitted for allocation above Rs, 10 crore and upto ₹ 250 crore, subject to minimum allotment of ₹ 5 crore per such investor;

- (iii) Minimum of 5 and maximum of 25 such investors shall be permitted for allocation above ₹ 250 crore, subject to minimum allotment of ₹ 5 crore per such investor.
- (b) Upto sixty per cent of the portion available for allocation to qualified institutional buyers shall be available to anchor investor(s) for allocation/ allotment.
- (c) One-third of the anchor investor portion shall be reserved for domestic mutual funds.
- (d) The bidding for Anchor Investors shall be open one day before the issue opening date.
- (e) Anchor Investors shall pay on application the same margin which is payable by other categories of investors, the balance to be paid within two days of the date of closure of the issue.
- (f) Allocation to Anchor Investors shall be completed on the day of bidding by Anchor Investors.
- (g) If the price fixed as a result of book building is higher than the price at which the allocation is made to Anchor Investor, the Anchor Investor shall bring in the additional amount. However, if the price fixed as a result of book building is lower than the price at which the allocation is made to Anchor Investor, the excess amount shall not be refunded to the Anchor Investor and the Anchor Investor shall take allotment at the price at which allocation was made to it.
- (h) The number of shares allocated to Anchor Investors and the price at which the allocation is made, shall be made available in public domain by the merchant banker before opening of the issue.
- (i) There shall be a lock-in of 30 days on the shares allotted to the Anchor Investor from the date of allotment in the public issue.
- (j) Neither the merchant bankers nor any person related to the promoter/ promoter group/merchant bankers in the concerned public issue can apply under Anchor Investor category. The parameters for selection of Anchor Investor shall be clearly identified by the merchant banker and shall be available as part of records of the merchant banker for inspection by SEBI.
- (k) The applications made by qualified institutional buyers under the Anchor Investor category and under the Non Anchor Investor category may not be considered as multiple applications.

APPLICATION SUPPORTED BY BLOCK AMOUNT

In its continuing endeavour to make the existing public issue process more efficient, SEBI has introduced a supplementary process of applying in public issues, viz., the “Applications Supported by Blocked Amount (ASBA)” process.

The ASBA process is available in all public issues made through the book building route. It shall co-exist with the current process, wherein cheque is used as a mode of payment.

ASBA is an application for subscribing to an issue, containing an authorization to block the application money in a bank account. The main features of ASBA process are as follows:

Self Certified Syndicate Bank

Self Certified Syndicate Bank (SCSB) is a bank which offers the facility of applying through the ASBA process. A bank desirous of offering ASBA facility shall submit a certificate to SEBI as per the prescribed format for inclusion of its name in SEBI's list of SCSBs.

A SCSB shall identify its Designated Branches (DBs) at which an ASBA investor shall submit ASBA and shall also identify the Controlling Branch (CB) which shall act as a coordinating branch for the Registrar of the issue, Stock Exchanges and Merchant Bankers. The SCSB, its DBs and CB shall continue to act as such, for all issues to which ASBA process is applicable. The SCSB may identify new DBs for the purpose of ASBA process and intimate details of the same to SEBI, after which SEBI will add the DB to the list of SCSBs maintained by it. The

SCSB shall communicate the following details to Stock Exchanges for making it available on their respective websites; these details shall also be made available by the SCSB on its website:

- (i) Name and address of all the SCSB.
- (ii) Addresses of DBs and CB and other details such as telephone number, fax number and email ids.
- (iii) Name and contacts details of a nodal officer at a senior level from the CB.

Eligibility of Investors

An Investor is eligible to apply through ASBA process, if he/she:

- (i) is a "Resident Retail Individual Investor";
- (ii) is bidding at cut-off, with single option as to the number of shares bid for;
- (iii) is applying through blocking of funds in a bank account with the SCSB;
- (iv) has agreed not to revise his/her bid;
- (v) is not bidding under any of the reserved categories.

ASBA Process

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

Obligations of the Issuer

The issuer shall ensure that adequate arrangements are made by the Registrar to the Issue to obtain information about all ASBAs and to treat these applications similar to non-ASBA applications while finalizing the basis of allotment, as per the procedure specified in the Guidelines.

Applicability of ASBA process

ASBA process is applicable to all book-built public issues which provide for not more than one payment option to the retail individual investors.

GREEN SHOE OPTION FACILITY

"Green Shoe Option" means an option of allocating shares in excess of the shares included in the public issue and operating a post-listing price stabilizing mechanism in accordance with the provisions of Regulation 45 of SEBI (ICDR) Regulations, 2009.

GSO in the system of IPO using book-building method was recognised by SEBI in India through its new guidelines on 14th August 2003 (vide SEBI/ CFD/DIL/DIP/ Circular No. 11). ICICI bank has used Green Shoe Option first time in its public issue through book building mechanism in India.

A company desirous of availing this option, should in the resolution of the general meeting authorising the public issue, seek authorisation also for the possibility of allotment of further shares to the 'Stabilising Agent' (SA) at the end of the stabilisation period.

The company should appoint one of the merchant bankers or book runners, amongst the issue management team, as the “stabilising agent” (SA), who will be responsible for the price stabilisation process, if required. The SA shall enter into an agreement with the issuer company, prior to filing of offer document with SEBI, clearly stating all the terms and conditions relating to this option including fees charged/expenses to be incurred by SA for this purpose.

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

The details of the agreements mentioned above should be disclosed in the draft prospectus, the draft Red Herring prospectus, Red Herring prospectus and the final prospectus. The agreements should also be included as material documents for public inspection. The lead merchant banker or the Lead Book Runner, in consultation with the SA, shall determine the amount of shares to be over-allotted with the public issue, subject to the maximum number specified above.

The draft prospectus, draft Red Herring prospectus, the Red Herring prospectus and the final prospectus should contain the following additional disclosures:

- (a) Name of the SA.
- (b) The maximum number of shares (as also the percentage vis-a-vis the proposed issue size) proposed to be over-allotted by the company.
- (c) The period, for which the company proposes to avail of the stabilisation mechanism.
- (d) The maximum increase in the capital of the company and the shareholding pattern post issue, in case the company is required to allot further shares to the extent of over-allotment in the issue.
- (e) The maximum amount of funds to be received by the company in case of further allotment and the use of these additional funds shall be disclosed in the offer document.
- (f) Details of the agreement/arrangement entered into by SA with the promoters or shareholders to borrow shares from the latter which *inter alia* shall include name of the promoters or shareholders, their existing shareholding, number and percentage of shares to be lent by them and other important terms and conditions including the rights and obligations of each party.
- (g) The exact number of shares to be allotted pursuant to the public issue, stating separately therein the number of shares to be borrowed from the promoters and over-allotted by the SA, and the percentage of such shares in relation to the total issue size.

In case of an initial public offer by a unlisted company, the promoters and pre-issue shareholders and in case of public issue by a listed company, the promoters and pre-issue shareholders holding more than 5% shares, may lend the shares subject to the provisions of this scheme. The SA should borrow shares from the promoters or the pre-issue shareholders of the issuer company or both, to the extent of the proposed over-allotment. However, the shares so referred shall be in dematerialized form only.

The allocation of these shares should be on pro rata basis to all the applicants.

The stabilisation mechanism should be available for the period disclosed by the company in the prospectus, which shall not exceed 30 days from the date when trading permission was given by the exchange(s).

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

The money received from the applicants against the over-allotment in the green shoe option should be kept in the GSO Bank Account, distinct from the issue account and shall be used for the purpose of buying shares from the market, during the stabilisation period.

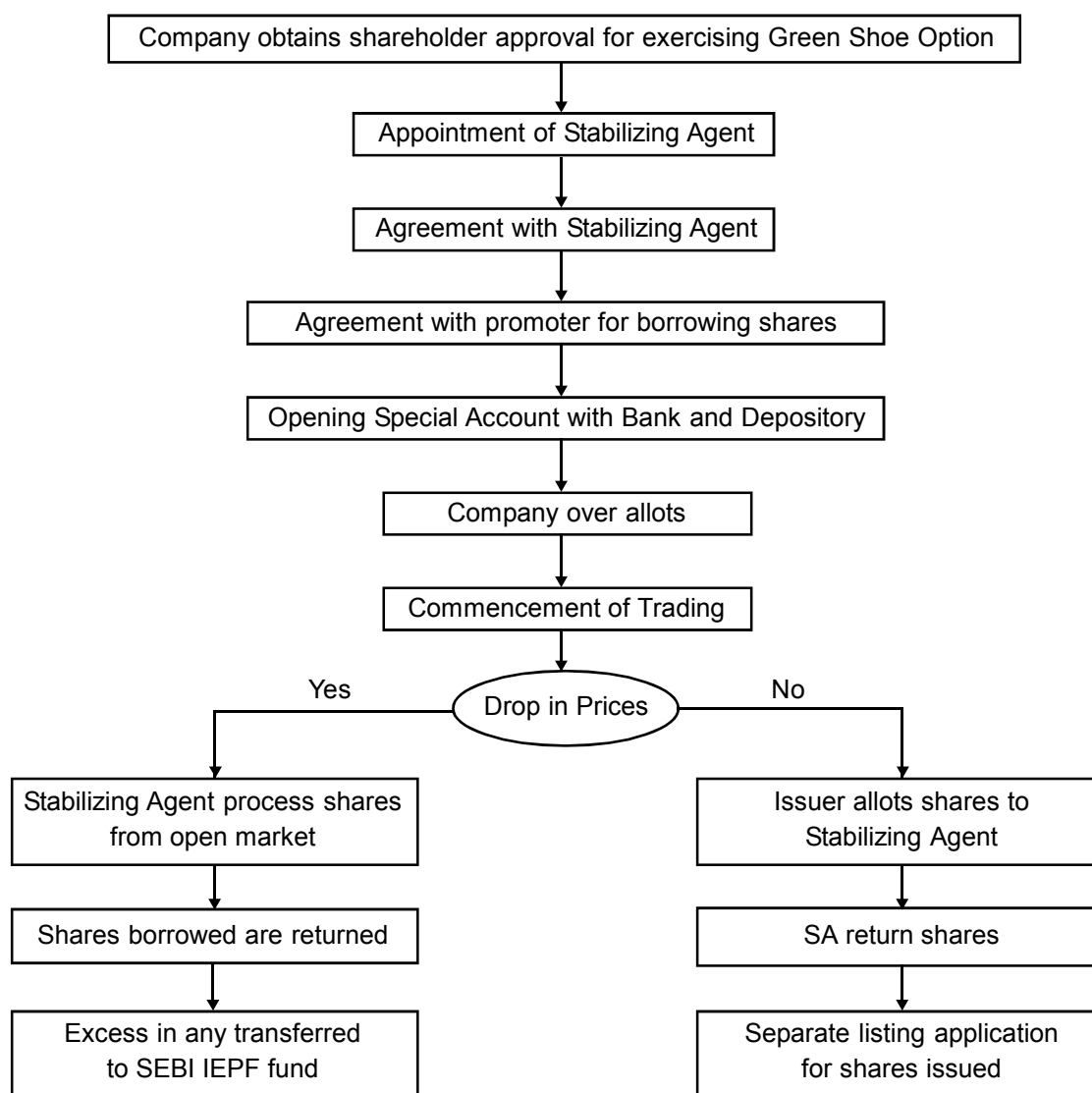
The shares bought from the market by the SA, if any during the stabilisation period, should be credited to the GSO Demat Account.

The shares bought from the market and lying in the GSO Demat Account should be returned to the promoters immediately, in any case not later than 2 working days after the close of the stabilisation period.

The prime responsibility of the SA should be to stabilise post listing price of the shares. To this end, the SA should determine the timing of buying the shares, the quantity to be bought, the price at which the shares are to be bought etc.

On expiry of the stabilisation period, in case of SA does not buy shares to the extent of shares over-allotted by the company from the market, the issuer company shall allot shares to the extent of the shortfall in dematerialized form to the GSO Demat Account, within five days of the closure of the stabilisation period. These shares shall be returned to the promoters by the SA in lieu of the shares borrowed from them and the GSO Demat Account shall be closed thereafter. The company shall make a final listing application in respect of these shares to all the exchanges where the shares allotted in the public issue are listed. The provisions relating to preferential issues shall not be applicable to such allotment.

GREEN SHOE OPTION PROCESS



The shares returned to the promoters as above, as the case may be, shall be subject to the remaining lock-in-period as provided in lock-in or pre-issue share capital of an unlisted company.

The SA shall remit an amount equal to (further shares allotted by the issuer company to the GSO Demat Account) (Issue Price) to the issuer company from the GSO Bank Account. The amount left in this account, if any, after this remittance and deduction of expenses incurred by the SA for the stabilisation mechanism, shall be transferred to the investor protection fund(s) established by SEBI. The GSO Bank Account shall be closed soon thereafter.

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

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

- in respect of each transaction effected in the course of the stabilising action, the price, date and time.
- the details of the promoters from whom the shares are borrowed and the number of shares borrowed from each; and
- details of allotments made.

The register must be retained for a period of at least three years from the date of the end of the stabilising period.

For the aforesaid, over allotment shall mean an allotment or allocation of shares in excess of the size of a public issue, made by the SA out of shares borrowed from the promoters or the pre-issue shareholders or both, in pursuance of green shoe option exercised by the company in accordance with the provisions of the scheme.

PROCEDURE FOR ISSUE OF SECURITIES

In the light of the provisions of the Companies Act and the guidelines issued by Government/SEBI under the Securities Contract (Regulations) Rules, 1956 and SEBI Act, 1992, the procedure for issue of securities to be followed by companies is given below. This procedure should be read along with the relevant SEBI regulations and provisions of the other Acts.

I. Issue of Shares to the Public

A company proposing to raise resources by a public issue should first select the type of securities i.e. shares and/or debentures to be issued by it. In case the company has applied for financial assistance to any of the financial/investment institutions, the requirement of the funds to be raised from the public is to be decided in consultation with the said institution while appraising the project of the company. The decision regarding the issue of shares to be made at par or premium should be taken. The various steps involved in public issue of shares are enumerated below:

1. Compliance with SEBI Regulations

Before making any issue of capital, it is to be ensured that the proposed issue complies with the eligibility norms and other provisions of SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009.

2. Holding of general meeting

A general meeting of the shareholders (annual or extraordinary) is to be convened for obtaining their consent to

the proposed issue of shares if the articles so require. In case the proposed issue requires any increase in authorised share capital (Section 61, 62, 64), alteration in capital clause of the Memorandum of Association (Section 13), alteration of the articles of association (Section 14) etc. the approvals for the same should also be obtained at the General Meeting.

3. Intimation to Stock Exchange

A copy of the Memorandum and Articles of Association of the company is to be sent to the Stock Exchanges where the shares are to be enlisted, for approval.

4. Appointment of managers to the issue

The Company issuing shares is to appoint one or more Merchant Bankers to act as managers to the public issue. The company should enter into a memorandum of understanding with the managers to the issue and decide the fees payable to them. Lead Managers are free to negotiate with the Managements their fee for handling the issue. If more than one Merchant Bankers are associated with the issue, the *inter-se* allocation of responsibility of each of them, shall be disclosed in the offer document.

5. Appointment of various other agencies

The company should in consultation with the Managers to the issue, decide upon the appointment of the following other agencies:

(a) Registrars to the Issue; (b) Collecting bankers to the Issue; (c) Advisors to the Issue; (d) Underwriters to the Issue; (e) Brokers to the Issue; (f) Printers; (g) Advertising Agents, Self Certified Syndicate Banks, etc.

These agencies should be registered with SEBI wherever registration is a condition for handling work by any of these agencies.

Consent of the aforesaid persons should be obtained in writing for acting in their respective capacities for filing, with the Registrar of Companies alongwith the prospectus.

6. Drafting of prospectus

Next step is to draft a prospectus in accordance with Section 26 of the Companies Act, 2013 and an abridged prospectus as required under Section 33(1) of the Companies Act, 2013. The prospectus should contain the disclosures as required by SEBI Regulations under Schedule VIII.

7. Approval of prospectus

The draft offer document alongwith the application form for issue of shares should be got approved by the solicitors/legal advisors of the company to ensure that it contains all disclosures and information as required by various statutes, rules, regulations, notifications, etc. The managers to the issue should also verify and approve the draft prospectus. The financial institutions providing loan facilities generally stipulate that the prospectus should be got approved by them. The company should in such a case, forward a copy of the draft prospectus for their verification and approval as well. The approval of underwriters should also be taken if they so require.

A copy of the draft offer document is also to be forwarded to the Registrar of Companies for its scrutiny and approval.

Merchant Bankers, acting as the Lead Manager to ensure that an offer document contain the disclosure requirements as specified by SEBI from time to time for the issue of securities. Also to ensure that an offer document provides a true, correct and fair view of the state of affairs of the company which are adequate for the investors to arrive at a well informed investment decision. The Merchant Bankers are required to submit the draft of the offer document along with Due Diligence Certificate to SEBI in the form specified within six weeks before the issue is scheduled to open for subscription. Further, they are held responsible for ensuring the compliance

with SEBI Rules, Regulations, Guidelines and requirements for other laws, for the time being in force. A check list containing aspects related to prospectus is given as under.

1. Check that a merchant banker holding a valid certificate of registration has been appointed to manage the issue and the lead merchant banker exercises the due diligence to satisfy himself about all the aspects of offering, veracity and adequacy of disclosures in the offer documents.
2. Check that a Memorandum of Understanding (MOU) has been entered into between lead merchant bankers and the issuer company specifying their mutual rights, liabilities and obligations relating to the issues.
3. Check that MOU does not contain any clause contrary to the provisions of the Companies Act, 2013 and SEBI (Merchant Bankers) Rules and Regulations, 1992 so as to diminish the liabilities and obligations of the lead merchant banker and issuer company.
4. Check that a draft offer document complete in all respects alongwith the Due Diligence Certificate, *inter-se* allocation of Responsibilities Certificate and a copy of Memorandum of Understanding and the requisite fee in accordance with SEBI (Merchant Bankers) Rules and Regulation, 1992 has been submitted to SEBI at least 30 days prior to the filing of prospectus with Registrar of Companies.
5. Check that the draft of offer document involving amount upto ₹ 50 crores has been referred to concerned regional offices of SEBI under the jurisdiction of which registered office of issuer company falls.
6. Check that a copy of the draft offer document has been filed simultaneously with all the Stock Exchanges where listing is sought for clearance and in principle approval of stock exchange for listing of securities has been obtained and furnished to SEBI within 30 days of filing of the draft offer document with the stock exchanges.
7. Check that the lead manager has handed over not less than 10 copies of the draft offer document to dealing offices of SEBI, 3 copies to Primary Market Department, SEBI Head Office and 25 copies to the Stock Exchange(s) where the issue is proposed to be listed.

Ensure that the lead merchant banker has also submitted the draft offer document on a computer floppy to the dealing officer of SEBI and Primary Market Department, SEBI Head Office. Also ensure that in case of issues made through book building process, the merchant banker has submitted a printed as well as soft copy of the offer document incorporating the Board of directors observations and also a bid cum application form to the Primary Market Department, SEBI head office atleast five days before opening of bidding.

8. Check that draft offer document filed with SEBI has been made public for a period of 21 days from the date of filing the offer document with SEBI. The lead managers/stock exchanges can charge an appropriate sum to the person requesting copy(ies) of draft prospects.
9. Check that after a period of 21 days from the date, draft offer document was made public, the lead manager has filed with SEBI a statement:
 - (a) giving a list of complaints received by it,
 - (b) a statement by it whether it is proposed to amend the draft prospectus or not, and
 - (c) highlighting the amendments.
10. Check that the lead merchant bankers have furnished to SEBI, a due diligence certificate alongwith draft offer document and has –
 - (a) Issued a certificate to SEBI that all the amendments suggested/ observations made by SEBI have been given effect to in the offer documents.

- (b) Furnished a 'fresh due diligence' certificate to SEBI at the time of filing of prospectus with the Registrar of Companies as per format specified.
 - (c) Furnished a fresh certificate immediately before the opening of the issue that no corrective action is needed.
 - (d) Furnished a fresh certificate after the issue has opened but before the issue is closed for subscription.
11. Check that the particulars as per audited statements contained in the offer document are not more than six months old from the issue opening date.
 12. However, in case of a Government company auditors' report in the offer document shall not be more than six months from the date of filing the offer document with the ROC or stock exchanges as the case may be.
 13. SEBI may within 30 days from the date of submission of draft offer document specify changes. Check that the changes specified by SEBI are duly considered by the merchant bankers before filing of the offer document with ROC.
 14. Check that the offer document or letter of offer has been filed with ROC or stock exchanges.
 15. Check that the two copies of final printed copy of the final offer document have been sent to dealing offices of SEBI at least within three days of filing offer document with Registrar of Companies/Stock Exchange as the case may be.
 16. Check that lead merchant banker has also submitted one final printed copy of the final offer document alongwith the computer floppy containing the final prospectus/letter of offer to SEBI.
 17. Check that the public issue offer documents and other issue material has been despatched to the various stock exchanges, brokers, underwriters, bankers/self certified syndicate banks to the issue etc. in advance as agreed upon.
 18. Check that 20 copies of the prospectus and application form has been despatched in advance of the issue opening date to various Investor Associations.
 19. Check that the following details about themselves certified as correct have been included by the lead merchant bankers in all the forwarding letters of offer document filed with any Department/office of SEBI.
 - (i) Registration number
 - (ii) Date of Registration/Renewal of Registration
 - (iii) Date of expiry of registration
 - (iv) If applied for renewal, date of application
 - (v) Any communication from SEBI prohibiting from acting as a merchant banker
 - (vi) Any inquiry/investigation being conducted SEBI.
 20. Also ensure that in the forwarding letters, the following details about the issuer company have been included while filing offer documents for public/ rights issue/buy-back/takeovers:
 - (i) Whether any promoter/director/group/associate company/entity of the issuer company and/or any company/entity with which any of the above is associated as promoter/director/partner/proprietor, is/was engaged in securities related business and registered with SEBI.
 - (ii) If any one or more of these persons/entities are/were registered with SEBI, their respective registration numbers.

- (iii) If registration has expired, reasons for non-renewal.
- (iv) Details of any enquiry/investigation conducted by SEBI at any time.
- (v) Penalties imposed by SEBI which includes deficiency/warning letter, adjudication proceedings, suspension/cancellation/prohibitory order.
- (vi) Outstanding fees payable to SEBI by these entities, if any.

8. Approval of board of directors to prospectus and other documents

After the concerned parties/agencies have approved the draft prospectus and the application form, the board of directors of the company should approve the final draft before filing with the Registrar of Companies. The company should, therefore, hold the meeting of the board of directors to transact the following business:

- (a) to approve and accept consent letters received from various parties agencies to act in their respective capacities;
- (b) to approve and accept appointment of underwriters, brokers, bankers to the issue registrar to the issue, solicitors and advocates to the issue, etc.
- (c) to accept the Auditors' Report for inclusion in the prospectus;
- (d) to approve the date of opening of subscription list as also earliest and latest dates for closing of subscription list with the authority in favour of any director for earlier closing if necessary.
- (e) to approve draft prospectus/draft abridged prospectus and the draft share application form.
- (f) to authorise filing of the prospectus signed by all the directors or their constituted attorneys with the Registrar of Companies.
- (g) to authorise any officer of the company to deliver the prospectus for registration with the Registrar of Companies and to carry out the corrections, if any, at the office of the Registrar of Companies.
- (h) to approve the format of the statutory announcement.

9. Making application to Stock Exchange(s) for permission to listing

Before filing prospectus with the Registrar of Companies the company should submit an application(s) to the Stock Exchange(s) for enlistment of securities offered to the public by the said issue [Section 40(1) of the Companies Act, 2013]. The fact that an application(s) has/have been made to the Stock Exchange(s) must be stated in the prospectus.

10. Printing and distribution of prospectus and application forms

After receipt of the intimation from Registrar of Companies regarding registration of prospectus, the company should take steps to issue the prospectus within 90 days of its registration with ROC. For the purpose, the first step is to get adequate number of prospectuses and application forms printed. The provisions of Section 33 of the Companies Act, 2013 should be kept in view in this regard which provide that no one shall issue any form of application for shares in or debenture of a company unless the form is accompanied by a memorandum containing such salient features of a prospectus as may be prescribed.

At least 2 weeks before the announcement is made in any newspaper, journal etc. requisite number of copies of the prospectus and application forms accompanied by the abridged prospectus should be distributed to the brokers, underwriters, merchant bankers, lead managers, bankers etc. to the issue.

11. Pricing**12. Promoters contribution and lock-in-period****13. Underwriting****14. Mandatory Collection Centres****15. Certificate relating to promoters' contribution**

SEBI Regulations require that atleast one day prior to the date of opening of the issue, a certificate from the Chartered Accountant to the effect that the promoters' contribution in its entirety has been brought in advance before the public issue opens should be forwarded to it. The certificate should be accompanied by a list of names and addresses of friends, relatives and associates who have contributed to the promoters' quota, along with the amount of subscription made by each of them.

16. Coordination with the bankers to the issue

The date of opening and closing of the subscription list should be intimated to all the collecting and controlling branches of the bank with whom the company has entered into an agreement for the collection of application forms. Further, the company should ensure that a separate bank account is opened for the purpose of collecting the proceeds of the issues as required by Section 40(3) of the Companies Act, 2013 and furnish to the controlling branches the resolution passed by the Board of directors for opening bank account.

17. Minimum subscription**18. Allotment of shares**

A return of allotment in Form PAS-3 of the Companies (Prospectus and Allotment of Securities) should be filed with the Registrar of Companies within 30 days of the date of allotment along with the fees as rules, 2014 specified in the Companies (Registration Offices and Fees) Rules, 2014.

19. Refund orders

The company shall disclose the mode in which it shall made refunds to applicants in the prospectus and abridged prospectus.

RIGHTS ISSUE

Rights issue as identified in the SEBI Regulations is an issue of capital under Section 62 of the Companies Act, 2013 to be offered to the existing shareholders of the company through a letter of offer.

This regulation is not applicable to the rights issue where the aggregate value of securities offered does not exceed ₹ 50 lakhs.

- A listed issuer company can not make any rights issue of securities, where the aggregate value of such securities, including premium, if any, exceeds ₹ 50 lakhs unless a draft letter of offer has been filed with SEBI, through a Merchant Banker, at least 30 days prior to the filing of the letter of offer with the Designated Stock Exchange (DSE).

However, in case of the rights issue where the aggregate value of the securities offered is less than ₹ 50 Lakhs, the company shall prepare the letter of offer in accordance with the disclosure requirements specified in these regulation and file the same with SEBI for its information and for being put on the SEBI website.

- An issuer company can not make any public issue of securities, unless a letter of offer has been filed with SEBI through a Merchant Banker, at least 30 days prior to the filing of the Prospectus with the Registrar of Companies (ROC).

However, if SEBI specifies changes or issues observations on letter of offer within 30 days from the date of receipt of the draft Prospectus by SEBI the issuer company or the Lead Manager to the Issue shall carry out such changes or comply with the observations issued by SEBI before filing the letter of offer with ROC.

- SEBI may specify changes or issue observations, if any, on the letter of offer only after receipt of copy of in-principle approval from all the stock exchanges on which the issuer company intends to list the securities proposed to be offered through the letter of offer.
- A Company can not make a rights issue of equity share or any security convertible at later date into equity share, unless all the existing partly paid-up shares have been fully paid or forfeited.
- A company can not make a rights issue of securities unless firm arrangements of finance through verifiable means towards 75% of the stated means of finance, excluding the amount to be raised through proposed Public/Rights issue, or through identifiable internal accruals have been made.
- A listed company whose equity shares are listed on a stock exchange, may freely price its equity shares and any security convertible into equity at a later date, offered through a rights issue.
- In case of a rights issue, issue price or price band may not be disclosed in the draft letter of offer filed with SEBI. The issue price may be determined anytime before fixation of the record date, in consultation with the Designated Stock Exchange
- In case of rights issue, the promoters shall disclose their existing shareholding and the extent to which they are participating in the proposed issue, in the offer document.
- A company can not make an issue of security through a public or rights issue unless a Memorandum of Understanding has been entered into between a lead merchant banker and the issuer company specifying their mutual rights, liabilities and obligations relating to the issue.
- In case a rights issue is managed by more than one Merchant Banker, the rights, obligations and responsibilities of each merchant banker shall be demarcated as specified in Chapter VI.
- In the case of rights issues, lead merchant banker shall ensure that the abridged letters of offer are dispatched to all shareholders at least three days before the date of opening of the issue.

However, if a specific request for letter of offer is received from any shareholder, the Lead Merchant Banker shall ensure that the letter of offer is made available to such shareholder.

- A disclosure to the effect that the securities offered through this rights issue shall be made fully paid up or may be forfeited within 12 months from the date of allotment of securities in the manner specified in these Regulations.
- A company can not make any further issue of capital during the period commencing from the submission of offer document to SEBI on behalf of the company for rights issues, till the securities referred to in the said offer document have been listed or application moneys refunded on account of non-listing or under subscription etc. unless full disclosures regarding the total capital to be raised from such further issues are made in the draft offer document.
- A Company can not issue any shares by way of rights unless it has made reservation of equity shares of the same class in favour of the holders of outstanding compulsorily convertible debt instruments ,if any, in proportion to the convertible part.
- The share so reserved for the holders of fully or partially compulsorily convertible debt instruments shall be issued at the time of conversion of such convertible debt instruments on the same terms at which the equity shares offered in the rights issue were issued.

- The Lead Merchant Banker shall ensure that in case of a rights issue, an advertisement giving the date of completion of despatch of letters of offer, shall be released in at least in an English National Daily with wide circulation, one Hindi National Paper and a Regional language daily circulated at the place where registered office of the issuer company is situated at least 3 days before the date of opening of the issue.
- An issuer company shall not withdraw rights issue after announcement of record date in relation to such issue.
- In cases where the issuer has withdrawn the rights issue after announcing the record date, the issuer company shall not make an application for listing of any securities of the company for a minimum period of 12 months from the record date.

However, shares resulting from the conversion of PCDs/ FCDs/ Warrants issued prior to the announcing of the record date in relation to rights issue may be granted listing by the concerned Stock exchange.

- Rights issues shall be kept open for at least 15 days and not more than 30 days.
- The quantum of issue whether through a rights or a public issue, shall not exceed the amount specified in the prospectus/ letter of offer.

However, an oversubscription to the extent of 10% of the net offer to public is permissible for the purpose of rounding off to the nearer multiple of 100 while finalising the allotment.

- If the issuer company does not receive the minimum subscription of ninety per cent of the issue (including devolvement of underwriters where applicable), the entire subscription shall be refunded to the applicants within fifteen days from the date of closure of the issue.
- If there is delay after the company becomes liable to pay the subscription amount (i.e. fifteen days after closure of the issue), the issuer company will pay interest to the subscribers at the rate of 15% per annum for the period of delay.
- The time period for finalization of basis of allotment in the rights issues is 15 days from the date of closure of the issue.
- The issuer company may utilise the funds collected in the rights issue only after the basis of allotment is finalized.

STEPS INVOLVED IN ISSUE OF RIGHTS SHARES

The various steps involved for issue of rights share are enumerated below:

1. Check whether the rights issue is within the authorised share capital of the company. If not, steps should be taken to increase the authorised share capital.
2. In case of a listed company, notify the stock exchange concerned the date of Board Meeting at which the rights issue is proposed to be considered at least 2 days in advance of the meeting.
3. Rights issue shall be kept open for at least 15 days and not more than 30 days.
4. Convene the Board meeting and place before it the proposal for rights issue.
5. The Board of directors should decide on the following matters:
 - (i) Quantum of issue and the proportion of rights shares.
 - (ii) Alteration of share capital, if necessary, and offering shares to persons other than existing holders of shares in terms of Section 62 of the Companies Act, 2013.
 - (iii) Fixation of record date.

- (iv) Appointment of merchant bankers and underwriters (if necessary).
- (v) Approval of draft letter of offer or authorisation of managing director/ company secretary to finalise the letter of offer in consultation with the managers to the issue, the stock exchange and SEBI.
- 6. Immediately after the Board Meeting notify the concerned Stock Exchanges about particulars of Board's of Directors decision.
- 7. If it is proposed to offer shares to persons other than the shareholders of the company, a General Meeting has to be convened and a resolution is to be passed for the purpose in terms of Section 62 of the Companies Act, 2013.
- 8. Forward 6 sets of letter of offer to concerned Stock Exchange(s).
- 9. Despatch letters of offer to shareholders by registered post.
- 10. Check that an advertisement giving date of completion of despatch of letter of offer has been released in at least an English National Daily, one Hindi National Paper and a Regional Language Daily where registered office of the issuer company is situated.
- 11. Check that the advertisement contains the list of centres where shareholders or persons entitled to rights may obtain duplicate copies of composite application forms in case they do not receive original application form alongwith the prescribed format on which application may be made.
- 12. The applications of shareholders who apply both on plain paper and also in a composite application form are liable to be rejected.
- 13. Make arrangement with bankers for acceptance of share application forms.
- 14. Prepare a scheme of allotment in consultation with Stock Exchange.
- 15. Convene Board Meeting and make allotment of shares.
- 16. Make an application to the Stock Exchange(s) where the company's shares are listed for permission of listing of new shares.

BONUS SHARES

A company may, if its Articles provide, capitalize its profits by issuing fully-paid bonus shares. The issue of bonus shares by a company is a common feature. When a company is prosperous and accumulates large distributable profits, it converts these accumulated profits into capital and divides the capital among the existing members in proportion to their entitlements. Members do not have to pay any amount for such shares. They are given free. The bonus shares allotted to the members do not represent taxable income in their hands. [*Commissioner of Income Tax, Madras v. A.A.V. Ramchandra Chettiar* (1964) 1 Mad CJ 281]. Issue of bonus shares is a bare machinery for capitalizing undistributed profits. The vesting of the rights in the bonus shares takes place when the shares are actually allotted and not from any earlier date.

ADVANTAGES OF ISSUING BONUS SHARES

- 1. Fund flow is not affected adversely.
- 2. Market value of the Company's shares comes down to their nominal value by issue of bonus shares.
- 3. Market value of the members' shareholdings increases with the increase in number of shares in the company.
- 4. Bonus shares is not an income. Hence it is not a taxable income.
- 5. Paid-up share capital increases with the issue of bonus shares.

Pursuant to the provisions of Section 52 of the Companies Act, 2013, securities premium account can be used in paying up unissued shares of the company to be issued to its members as fully-paid bonus shares. Other free reserves created from out of the profits actually earned during earlier years like general reserve, capital redemption reserve account, devolvement rebate reserve etc. can be utilised by company for issue of fully paid bonus shares to its members.

There are no guidelines on issuing bonus shares by private or unlisted companies. However, SEBI has notified Regulations for Bonus Issue which are contained in Chapter IX of SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009 with regard to bonus issues by listed companies.

When a company has accumulated free reserves and is desirous of bridging the gap between the capital and fixed assets, it issues bonus shares to its equity shareholders. Such an issue would not place any fresh funds in the hands of the company. On the contrary, after a bonus issue it would become necessary for the company to earn more to effectively service the increased capital. The shareholder will, however, be benefitted by way of increased return on investment and increased number of shares in their hands.

The following conditions must be satisfied before issuing bonus shares:

- (a) Bonus Issue must be authorised by the articles of the company. Such a provision is generally there in articles of almost all the companies as they adopt Table A. Schedule I of the Companies Act, 2013 (Regulation 96) of ICDR Regulations, 2009.
- (b) Bonus Issue must be sanctioned by shareholders in general meeting on recommendation of the Board of directors of the company.
- (c) Regulations issued by SEBI must be complied with.
- (d) Authorised Capital must be increased where necessary.

SEBI REGULATIONS PERTAINING TO BONUS ISSUE

1. Out of Free Reserves

The bonus issue is to be made out of free reserves built out of the genuine profits or securities premium collected in cash only.

2. Revaluation Reserves

The reserves created by revaluation of fixed assets should not be capitalised. These reserves are in fact capital reserves. However, if the assets are subsequently sold and the profits are realised, such profits could be utilised for capitalisation purposes. In fact the Government has in the past approved issue of bonus shares out of capital reserves representing realised capital profits.

3. Bonus Issue not to be in lieu of Dividend

Bonus issue should not be made in lieu of dividend.

4. Fully Paid Shares

If there are any partly paid-up shares outstanding on the date of allotment, these shares should be made fully paid-up before the bonus issue is made.

5. No Default in respect of Fixed Deposits/Debentures

The company should not have defaulted in the payment of any interest or principal in respect of its fixed deposits, debt securities issued by it.

6. Statutory Dues of the Employees

The company should not have defaulted in the payment of its statutory dues to the employees such as contribution to provident fund, gratuity, bonus.

7. Implementation of Proposal within fifteen days

A company which announces bonus should be implement within fifteen days issue after the approval of board of directors and does not require shareholders' approval for capitalisation of profits or reserves for making bonus issue as per the Articles of Association and shall not have the option of changing the decision.

However, where the company is required to seek shareholders' approval for capitalisation of profits or reserves for making bonus issue as per the Articles of Association, the bonus issue should be implemented within two months from the date of the meeting of the board of directors wherein the decision to announce bonus was taken subject to shareholders' approval.

8. Provision in Articles of Association

The Articles of Association of the Company should provide for capitalisation of reserves and if not a General Meeting of the company is to be held and a special resolution making provisions in the Articles of Association for capitalisation should be passed.

9. Authorised Capital

If consequent upon the issue of bonus shares, the subscribed and paid-up capital of the company exceed the authorised share capital, a General Meeting of the company should be held to pass necessary resolution for increasing the authorised capital.

STEPS IN ISSUE OF BONUS SHARES

A company issuing bonus shares should ensure that the issue is in conformity with the Regulations for bonus issue laid down by SEBI (ICDR) Regulations, 2009.

The procedure for issue of bonus shares by a listed company is enumerated below:

1. Ensure that bonus issue has been made out of free reserves built out of the genuine profits or securities premium collected in cash only.
2. Ensure that reserves created by revaluation of fixed assets are not capitalised.
3. Ensure that the company has not defaulted in payment of interest or principal in respect of fixed deposits or debt securities issued by it or in respect of the payment of statutory dues of the employees such as contribution to provident fund, gratuity, bonus etc.
4. Ensure that the bonus issue is not made in lieu of dividend.
5. There should be a provision in the articles of association of the company permitting issue of bonus shares; if not, steps should be taken to alter the articles suitably.
6. The share capital as increased by the proposed bonus issue should be well within the authorised capital of the company; if not, necessary steps have to be taken to increase the authorised capital.
7. Finalise the proposal and fix the date for the Board Meeting for considering the proposal and for authorising the taking up of incidental and attendant matters.
8. If there are any partly paid-up shares, ensure that these are made fully paid-up before the bonus issue is recommended by the Board of directors.
9. The date of the Board Meeting at which the proposal for bonus issue is proposed to be considered should be notified to the Stock Exchange(s) where the company's shares are listed.

10. Hold the Board Meeting and get the proposal approved by the Board of directors.
11. The resolution to be passed at the General Meeting should also be approved by the Board of Directors in its meeting. The intention of the Board of directors regarding the rate of dividend to be declared in the year after the bonus issue should be indicated in the resolution for bonus issue to be passed by members in general meeting.
12. Immediately after the Board meeting intimate the Stock Exchange(s) regarding the outcome of the Meeting.
13. Ensure that the company has announced bonus issue after the approval of Board of Directors and did not require shareholders' approval for capitalization of profits or reserves for making bonus issue as per the Article of Association, had implemented bonus issue within fifteen days from the date of approval of the issue by the board of directors of the company and must not have the option of changing the decision.

However, where the company was required to seek shareholders' approval for capitalization of profits or reserves for making bonus issue as per the Article of Association, the bonus issue has implemented within two months from the date of the meeting of the Board of Directors where in the decision to announce bonus was taken subject to shareholders' approval.

14. Arrangements for convening the general meeting should be made keeping in view the requirements of the Companies Act, 2013 with regard to length of notice, explanatory statement etc. Also three copies of the notice should be sent to the Stock Exchange(s) concerned.
15. Hold the general meeting and get the resolution for issue of bonus shares passed by the members. A copy of the proceedings of the meeting is to be forwarded to the concerned Stock Exchange(s).
16. In consultation with the Regional Stock Exchange fix the date for closure of register of members or record date and get the same approved by the Board of directors. Issue a general notice under Section 91 of Companies Act, 2013 in respect of the fixation of the record date in two newspapers one in English language and other in the language of the region in which the Registered Office of the company is situated.
17. Give 7 days notice to the Stock Exchange(s) concerned before the date of book closure/record date.
18. After the record date process the transfers received and prepare a list of members entitled to bonus shares on the basis of the register of members as updated. This list of allottees is to be approved by the Board or any Committee thereof. The list usually serves as allotment list and on this basis the allotment is to be made to the eligible members.
19. File return of allotment with the Registrar of Companies within 30 days of allotment (Section 39 of the Companies Act, 2013). Also intimate Stock Exchange(s) concerned regarding the allotments made.
20. Ensure that the allotment is made within fifteen days of the date on which the Board of directors approved the bonus issue.
21. Submit an application to the Stock Exchange(s) concerned for listing the bonus shares allotted.

PREFERENTIAL ISSUE BY EXISTING LISTED COMPANIES

Preferential issue means issuance of equity shares to promoter group or selected investors. It covers allotment of fully convertible debentures, partly convertible debentures or any other financial instruments that could be converted into equity shares at a later date. The investors could be institutional investors, private equity investors, high net-worth individuals, or companies.

Preferential issue is one of the key sources of funding for companies. It has its own advantages and disadvantages.

One of the biggest advantages of a preferential issue is that the company can raise money quickly and cheaply compared with other means of raising money, say IPO or issue of shares on a rights basis.

On the other hand, preferential issues and private placement is only for selected class of investors and not for the retail investors. It is like a wholesale market, where institutions with financial clout are allowed to participate. This deprives investment opportunity to the retail investors.

SEBI (ICDR) REGULATIONS, 2009 REGARDING PREFERENTIAL ISSUE

1. Applicability

The preferential issue of equity shares/Fully Convertible Debentures (FCDs)/ Partly Convertible Debentures (PCDs) or any other financial instruments which would be converted into or exchanged with equity shares at a later date, by listed companies whose equity share capital is listed on any stock exchange, to any select group of persons under Section 62 of the Companies Act, 2013 on private placement basis is governed by these Regulations.

2. Pricing of the issue

Regulation 76 lays down the pricing of equity share in case of frequently traded shares

- (i) Where the equity shares of the company have been listed on a stock exchange for a period of twenty six weeks or more as on the relevant date, the issue of equity shares on preferential basis is being made at a price not less than higher of the following:
 - (a) The average of the weekly high and low of the volume weighted average price of the related equity shares quoted on the stock exchange during the twenty six weeks preceding the relevant date;
 - OR
 - (b) the average of the weekly high and low of the volume weighted average price of the related equity shares quoted on a stock exchange during the two weeks preceding the relevant date.
- (ii) Where the equity shares of a company have been listed on a stock exchange for a period of less than twenty six weeks as on the relevant date, the issue of shares on preferential basis has been made at a price not less than the higher of the following:
 - (a) The price at which shares were issued by the company in its IPO or the value per share arrived at in a scheme of arrangement under Section 230 to 232 of the Companies Act, 2013, pursuant to which shares of the company were listed , as the case may be;
 - OR
 - (b) The average of the weekly high and low of the volume weighted average price of the related shares quoted on the stock exchange during the period shares have been listed preceding the relevant date;
 - OR
 - (c) The average of the weekly high and low of the volume weighted average price of the related shares quoted on a stock exchange during the two weeks preceding the relevant date."

Where the price of the equity shares is determined in terms of provision (ii), such price shall be recomputed by the issuer on completion of twenty six weeks from the date of listing on a recognized stock exchange with reference to the average of weekly high and low of the volume weighted average price of the related equity shares quoted on the recognized stock exchange during these twenty six weeks and if such recomputed price is higher than the price paid on allotment, the difference shall be paid by the allottees to the issuer.

An issue of shares on preferential basis to Qualified Institutional Buyers not exceeding five in

numbers all be made at a price not less than the average of the weekly high and low of the volume weighted average price of the related shares quoted on a stock exchange during the two weeks preceding the relevant date.

Regulation 76A lays down the pricing of equity shares in case of Infrequently traded shares

Where the shares are not frequently traded, the price determined by the company shall take into account valuation parameters including book value, comparable trading multiples, and such other parameters as are customary for valuation of shares of such companies.

However, the company shall submit a certificate stating that the company is in compliance of this regulation, obtained from an independent merchant banker or an independent chartered accountant in practice having a minimum experience of ten years, to the stock exchange where the equity shares of the company are listed.

Regulation 76B lay down the adjustments in pricing in case of frequently or infrequently traded shares

The price determined for preferential issue in accordance with regulation 76 or regulation 76A, shall be subject to appropriate adjustments, if the company :

- (a) makes an issue of equity shares by way of capitalization of profits or reserves, other than by way of a dividend on shares;
- (b) makes a rights issue of equity shares;
- (c) consolidates its outstanding equity shares into a smaller number of shares;
- (d) divides its outstanding equity shares including by way of stock split;
- (e) re-classifies any of its equity shares into other securities of the issuer;
- (f) is involved in such other similar events or circumstances, which in the opinion of the concerned stock exchange, requires adjustments.

Relevant date means the date thirty days prior to the date on which the meeting of general body of shareholders is held, in terms of Section 62 of the Companies Act, 2013.

Payment of consideration

- Full consideration of specified securities other than warrants issued under this Chapter shall be paid by the allottees at the time of allotment of such specified securities.

However, preferential issue of specified securities pursuant to a scheme of corporate debt restructuring as per the corporate debt restructuring framework specified by RBI, the allottee may pay the consideration in terms of such scheme.

- An amount equivalent to at least 25% of the consideration determined in terms of regulation 76 shall be paid against each warrant on the date of allotment of warrants.
- The balance 75% of the consideration shall be paid at the time of allotment of equity shares pursuant to exercise of option against each such warrant by the warrant holder.
- In case the warrant holder does not exercise the option to take equity shares against any of the warrants held by him, the consideration paid in respect of such warrant shall be forfeited by the issuer.
- The company shall ensure that the consideration of specified securities, if paid in cash, shall be received from respective allottee's bank account.
- The company shall submit a certificate of the statutory auditor to the stock exchange where the equity shares of the company are listed stating that the company is in compliance of above provisions and the relevant documents thereof are maintained by the company as on the date of certification.

Disclosures

- The company shall, in addition to the disclosures required under section 102 of the Companies Act, 2013 or any other applicable law, disclose the following in the explanatory statement to the notice for the general meeting proposed for passing special resolution:
 - (a) The objects of the preferential issue;
 - (b) The proposal of the promoters, directors or key management personnel of the issuer to subscribe to the offer;
 - (c) The shareholding pattern of the issuer before and after the preferential issue;
 - (d) The proposed time within which the preferential issue shall be completed;
 - (e) The identity of the natural persons who are the ultimate beneficial owners of the shares proposed to be allotted and/or who ultimately control the proposed allottees, the control, if any, in the issuer consequent to the preferential issue.

However, if there is any listed company, mutual fund, bank or insurance company in the chain of ownership of the proposed allottee, no further disclosure will be necessary.

 - (f) An undertaking that the issuer shall re-compute the price of the specified securities in terms of the provision of these regulations where it is required to do so.
 - (g) An undertaking that if the amount payable on account of the re-computation of price is not paid within the time stipulated in these regulations, the specified securities shall continue to be locked- in till the time such amount is paid by the allottees.
 - (h) Disclosures, similar to disclosures specified in Part G of schedule VIII, if the issuer or any of its promoters or directors is a wilful defaulter.
- The issuer shall place a copy of the certificate of its statutory auditor before the general meeting of the shareholders, considering the proposed preferential issue, certifying that the issue is being made in accordance with the requirements of these regulations. Where specified securities are issued on a preferential basis to promoters, their relatives, associates and related entities for consideration other than cash, the valuation of the assets in consideration for which the equity shares are issued shall be done by an independent qualified valuer, which shall be submitted to the recognised stock exchanges where the equity shares of the issuer are listed.
- The recognised stock exchange is not satisfied with the appropriateness of the valuation, it may get the valuation done by any other valuer and for this purpose it may obtain any information, as deemed necessary, from the issuer. The special resolution shall specify the relevant date on the basis of which price of the equity shares to be allotted on conversion or exchange of convertible securities shall be calculated.

5. Tenure of Convertible Securities

The tenure of the convertible securities of the issuer does not exceed beyond 18 months from the date of their allotment.

6. Lock-in-period

- (i) The specified securities allotted on a preferential basis to the promoter or promoter group and the equity shares allotted to such promoter or promoter group pursuant to exercise of options attached to warrants issued on preferential basis are to promoter or promoter group subjected to lock in period of three years from the date of trading approval granted.

However, not more than 20% of the total capital of the company, should be locked in for a period of three years from the date of trading approval .

Further, the equity shares allotted in excess of twenty percent pursuant to exercise of options attached to warrants issued on preferential basis to promoter/promoter group of the issuer, should be locked-in for a period of one year from the date of trading approval.

- (ii) The specified securities allotted on preferential basis and the equity shares allotted pursuant to exercise of options attached to warrants issued on preferential basis to any person other than the promoter/promoter group of the issuer should be locked in for a period of one year from the date of their allotment.
- (iii) Shares acquired by conversion of the convertible instruments other than warrants should be locked in for a period as reduced by the extent the convertible instrument other than warrants have already been locked in.
- (iv) The lock-in period in respect of shares issued on preferential basis pursuant to a scheme approved under Corporate Debt Restructuring framework of Reserve Bank of India, shall commence from the date of trading approval and has been continued for a period of one year and in case of allotment of partly paid up shares the lock-in period shall commence from the date of trading approval and continue for a period of one year from the date when shares become fully paid up.
- (v) The entire pre preferential allotment shareholding of such allottees shall be under lock-in from the relevant date upto a period of six months from the date of preferential allotment.

7. Allotment Pursuant to Shareholders Resolutions

- (i) Allotment pursuant to special resolution shall be completed within a period of fifteen days from the date of passing of the resolution.

However, where any application for exemption for the allotment on preferential basis is pending on account of pendency of any approval of such allotment by any regulatory authority or the Central Government; the allotment shall be completed within 15 days from the date of such approval.

However, SEBI has granted relaxation to the issuer in terms of the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011, the preferential allotment of shares, fully convertible debentures and partly convertible debentures, shall be made by it within such time as may be specified by SEBI in its order granting relaxation.

- (ii) If the allotment of specified securities is not completed within 15 days from the date of special resolution, a fresh special resolution shall be passed and the relevant date for determining the price of specified securities under this Chapter will be taken with reference to the date of latter special resolution.
- (iii) Where a preferential allotment is made that attracts an obligation to make an open offer for shares of the company under SEBI (Substantial Acquisition of Shares and Takeovers) Regulation, 2011, and there is no offer made of regulation 20 of the SEBI (Substantial Acquisition of Shares and Takeovers) Regulation, 2011, the period of 15 days shall be counted from the expiry of the period specified in regulation 20 or date of receipt of all statutory approvals required for the completion of an open offer under the SEBI (Substantial Acquisition of Shares and Takeovers) Regulation, 2011.

However, if an offer is made under regulation 20 of the SEBI (Substantial Acquisition of Shares and Takeovers) Regulation, 2011, the period of 15 days shall be counted from the expiry of the offer period as defined in the SEBI (Substantial Acquisition of Shares and Takeovers) Regulation, 2011.

Further that the provisions of this regulation shall not apply to an offer made under regulation 20 of the SEBI (Substantial Acquisition of Shares and Takeovers) Regulation, 2011, pursuant to a preferential allotment.

- (iv) Allotment shall only be made in dematerialised form. The requirement of allotment in dematerialised form shall also be applicable for the equity shares to be allotted pursuant to exercise of option attached to warrant or conversion of convertible securities.

8. Transferability of locked-in specified securities and warrants issued on preferential basis

Any Specified securities held by promoters and locked-in as prescribed in regulation, may be transferred among promoters or promoter group or to a new promoter or persons in control of the company. Lock-in on such specified securities shall continue for the remaining period with the transferee. The specified securities allotted on preferential basis shall not be transferred by the allottee till trading approval is granted for such securities by all the recognised stock exchanges where the equity shares of the issuer are listed.

“total capital of the issuer” means equity share capital issued by way of public issue or rights issue including equity shares issued pursuant to conversion of specified securities which are convertible; and specified securities issued on a preferential basis to promoter or promoter group.

“the date of trading approval” means the latest date when trading approval has been granted by all the recognised stock exchanges where the equity shares of the issuer are listed, for specified securities allotted as per the provisions of this Chapter.

Further that requirement of allotment within fifteen days shall not apply to allotment of specified securities on preferential basis pursuant to a scheme of corporate debt restructuring as per the corporate debt restructuring framework specified by RBI.

9. Use of Issue Proceeds

The details of all monies utilised out of the preferential issue proceeds should be disclosed under an appropriate head in the balance sheet of the company indicating the purpose for which such monies have been utilised. The details of unutilised monies should also be disclosed under a separate head in the balance sheet of the company indicating the form in which such utilised monies have been invested.

10. Other Requirements

- A special resolution is required to be passed by its shareholders.
- All the equity shares if any, held by the proposed allottees in the issuer are in dematerialised form.
- An issuer cannot make preferential issue of securities to any person who has sold any equity shares of the issuer during the six months proceeding the relevant date.
- A listed company shall not make any preferential issue of specified securities unless it is in compliance with the conditions for continuous listing.
- A listed company shall not make any preferential allotment of specified securities unless it has obtained the Permanent Account Number of the proposed allottees.

NON-APPLICABILITY

(1) These regulations are not applicable in case of the following:

- (a) pursuant to conversion of loan or option attached to convertible debt instruments in terms of Sections 62 of the Companies Act, 2013.
- (b) pursuant to a scheme approved by a Tribunal under Section 230 to 232 of the Companies Act, 2013. However, the pricing provisions of this Chapter shall apply to the issuance of shares under schemes mentioned in clause (b) in case of allotment of shares only to a select group of shareholders or shareholders of unlisted companies pursuant to such schemes;
- (c) in terms of the rehabilitation scheme approved by the Board of Industrial and Financial Reconstruction under the Sick Industrial Companies (Special Provisions) Act, 1985 or the resolution plan approved by the Tribunal under the Insolvency and Bankruptcy Code, 2016, whichever applicable.

However, the lock-in provisions of this Chapter shall apply to preferential issue of equity shares mentioned in clause (c).

(2) Pricing and lock-in provisions of SEBI (ICDR) Regulations, 2009 shall not apply to equity shares allotted to any financial institution within the meaning of sub-clauses (ia) and (ii) of Clause (h) of Section 2 of the Recovery of Debts due to Banks and Financial Institutions Act, 1993.

(3) Disclosure and pricing relating to a preferential issue of equity shares and compulsorily convertible debt instruments, whether fully or partly, where SEBI has granted relaxation to the issuer in terms of the SEBI

(Substantial Acquisition of Shares and Takeovers) Regulations, 2011, if adequate disclosures about the plan and process proposed to be followed for identifying the allottees are given in the explanatory statement to notice for the general meeting of shareholders.

(4) Criteria relating to Lock –in and selling of equity shares during six months preceding the preferential issue shall not apply to preferential issue of specified securities where the proposed allottee is a Mutual Fund registered with SEBI or Insurance Company registered with Insurance Regulatory and Development Authority of India or a Scheduled Bank listed under the Second Schedule of the Reserve Bank of India Act, 1934 or a Public Financial Institution as defined in clause 72 of section 2 of the Companies Act, 2013.

(5) The provisions of the Chapter shall not apply where the preferential issue of specified securities is made to the lenders pursuant to conversion of their debt, as part of a debt restructuring scheme implemented in accordance with the guidelines specified by RBI, subject to the following conditions:

- a) the guidelines for determining the conversion price have been specified by RBI in accordance with which the conversion price shall be determined and which shall be in compliance with the applicable provisions of the Companies Act, 2013;
- b) the conversion price shall be certified by two independent qualified valuers, and “valuer” shall be a person who is registered under section 247 of the Companies Act, 2013 and the relevant Rules framed thereunder.

However, till such date on which section 247 of the Companies Act, 2013 and the relevant Rules come into force, valuer shall mean an independent merchant banker registered with SEBI or an independent chartered accountant in practice having a minimum experience of ten years;

- c) specified securities so allotted shall be locked-in for a period of one year from the date of their allotment.

However, for the purpose of transferring the control, the lenders may transfer the specified securities allotted to them before completion of the lock-in period subject to continuation of the lock-in on such securities for the remaining period, with the transferee;

- d) the lock-in of equity shares allotted pursuant to conversion of convertible securities issued on preferential basis shall be reduced to the extent the convertible securities have already been locked-in;
- e) the applicable provisions of the Companies Act, 2013 are complied with, including the requirement of special resolution.”

(6) The provisions of the Chapter shall not apply where the preferential issue, if any, of specified securities is made to person(s) at the time of lenders selling their holding of specified securities or enforcing change in ownership in favour of such person(s) pursuant to a debt restructuring scheme implemented in accordance with the guidelines specified by RBI, subject to the following conditions:

- a) the guidelines for determining the issue price have been specified by RBI in accordance with which the issue price shall be determined and which shall be in compliance with the applicable provisions of the Companies Act, 2013;
- b) the issue price shall be certified by two independent qualified valuers, and “valuer” shall be a person who is registered under section 247 of the Companies Act, 2013 and the relevant Rules framed thereunder.

However, till such date on which section 247 of the Companies Act, 2013 and the relevant Rules come into force, valuer shall mean an independent merchant banker registered with SEBI or an independent chartered accountant in practice having a minimum experience of ten years;

- c) the specified securities so allotted shall be locked-in for a period of at least three years from the date of their allotment;

- d) the lock-in of equity shares allotted pursuant to conversion of convertible securities issued on preferential basis shall be reduced to the extent the convertible securities have already been locked-in;
- e) a special resolution has been passed by shareholders of the issuer before the preferential issue;
- f) the issuer shall, in addition to the disclosures required under the Companies Act, 2013 or any other applicable law, disclose the following information pertaining to the proposed allottee(s) in the explanatory statement to the notice for the general meeting proposed for passing the special resolution as stipulated at clause (e) of this sub regulation:
 - a. the identity including that of the natural persons who are the ultimate beneficial owners of the shares proposed to be allotted and/ or who ultimately control the proposed allottee(s);
 - b. the business model;
 - c. a statement on growth of business over the period of time;
 - d. summary of audited financials of previous three financial years;
 - e. track record in turning around companies, if any;
 - f. the proposed roadmap for effecting turnaround of the issuer.
- g) the applicable provisions of the Companies Act, 2013 are complied with.

Procedure to deal with cases prior to April 01, 2014 involving offer / allotment of securities to more than 49 up to 200 investors in a financial year

Prior to April 01, 2014, offers of securities - shares and debentures - by companies to more than 49 persons were deemed to be public offers. SEBI has initiated penal action on receipt of specific complaints against the companies offering such securities without complying with the relevant provisions of the Companies Act, 1956 and applicable SEBI Guidelines / Regulations governing a public issue. Under the new Companies Act, 2013, post April 01, 2014, any offer or allotment of securities shall be construed as public issue if the number of offerees / allottees exceeds 200 persons in a financial year, excluding certain class of subscribers.

Considering the higher cap for private placement provided in the Companies Act, 2013, SEBI has clarified vide its Circular dated December 31, 2015 that in respect of earlier cases involving issuance of securities to more than 49 persons but up to 200 persons in a financial year, the companies may avoid penal action if they provide the investors with an option to surrender the securities and get the refund amount at a price not less than the amount of subscription money paid along with 15% interest p.a. thereon or such higher return as promised to investors.

Refund procedure

- The process followed by companies for providing option to their security holders to surrender securities and obtain refund shall be supported by proof of dispatch through Registered or Speed Post by India Post or proof of delivery of letters if effected through any other mode.
- The refund to security holders who have opted for such surrender shall be made only through banking channels through crossed account payee cheque / crossed demand draft / internet banking channels to enable audit trail.
- Companies are allowed to adjust the amounts already paid to the allottees either as interest / dividend or otherwise from the amount of refund to be paid to the investors.
- In case of transfer of securities by the original allottees, the option for refund shall be provided to the current holders of the securities.

Certification

The company shall submit a certificate from an independent peer reviewed practising chartered accountant/practising

Company Secretary certifying compliance as mentioned above. The certificate as provided above shall state that the certification has been made after verifying various documentary evidences including proof of dispatch / delivery of letters, response of investors, complaints from investors, bank statements of the company, etc.

QUALIFIED INSTITUTIONS PLACEMENT

A Qualified Institutions Placement means allotment of eligible securities by a listed issuer to qualified institutional buyers on private placement basis in terms of SEBI (ICDR) Regulations. This QIP is different from offer of securities to qualified institutional buyers in an IPO.

Eligible securities for the purpose of QIP

Eligible Securities include equity shares, non-convertible debt instruments along with warrants and convertible securities other than warrants.

QUALIFIED INSTITUTIONAL BUYER

A QIB means –

- (i) A mutual fund, venture capital fund, alternative investment fund and foreign venture capital investor registered with SEBI;
- (ii) A foreign portfolio investor other than Category III foreign portfolio investor registered with SEBI;
- (iii) A public financial institution as defined in section 2(72) of the Companies Act, 2013;
- (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;
- (x) National Investment Fund set up by the Government of India published in the Gazette of India;
- (xi) Insurance funds set up and managed by army, navy or air force of the Union of India;
- (xii) Insurance funds set up and managed by Department of Posts, India;
- (xiii) Systemically Important Non-Banking Financial Companies.

Relevant date

In case of allotment of equity shares, the date of the meeting in which the board of directors or the committee of directors duly authorised by the board of directors of the issuer decides to open the proposed issue.

In case of allotment of eligible convertible securities, either the date as mentioned above or the date on which the holders of such convertible securities become entitled to apply for the equity shares.

Systemically Important Non-Banking Financial Company

A non-banking financial company registered with the Reserve Bank of India and having a net-worth of more than five hundred crore rupees as per the last audited financial statements.

Conditions for making QIP

A listed issuer can make qualified institutions placement subject to the following conditions:

- A special resolution approving the issue is required to be passed by its shareholders.

- Prior to the date of issuance of notice to its shareholders for convening the meeting to pass the special resolution, the equity shares of the same class, which are proposed to be allotted through QIP, are listed on a recognised stock exchange having nation wide trading terminal for a period of at least one year.
- If an issuer, being a transferee company in a scheme of merger, de-merger, amalgamation or arrangement sanctioned by a Tribunal under sections 230 to 232 of the Companies Act, 2013, makes QIP, the period for which the equity shares of the same class of the transferor company were listed on a stock exchange having nation wide trading terminals are also eligible to be considered for the purpose of computation of the period of one year.
- It is in compliance with the requirement of minimum public shareholding specified in the Securities Contracts (Regulations) Rules, 1957.
- In the special resolution, it shall be, among other relevant matters, the resolution must specify the relevant date and also specify that the allotment is proposed to be made through QIP.

Intermediaries involved in QIP and their roles

A qualified institutions placement is required to be managed by merchant banker(s) who will exercise due diligence. While seeking in-principle approval for listing of the eligible securities issued under qualified institutions placement, the merchant banker furnishes to each stock exchange on which the same class of equity shares of the issuer are listed, a due diligence certificate regarding compliance of ICDR regulations and stating that the eligible securities are being issued under qualified institutions placement.

Placement document

‘Placement Document’ means document prepared by Merchant Banker for the purpose of Qualified Institutions placement and contains all the relevant and material disclosures to enable QIBs to make an informed decision.

Disclosures required to be made in Placement Document

- The qualified institutions placement is required to be made on the basis of a placement document which contains all material information, including those specified in ICDR Regulations and disclosures similar to disclosures specified in Part G of schedule VIII shall be, if applicable.
- The placement document needs to be serially numbered and copies are required to be circulated only to select Investors.
- The issuer, while seeking in-principle approval from the recognised stock exchange is required to furnish a copy of the placement document, a certificate confirming compliance with the provisions ICDR Regulations along with any other documents required by the stock exchange.
- The placement document is required to be placed on the website of the issuer and concerned stock exchange with a disclaimer to the effect that it is in connection with a qualified institutions placement and that no offer is being made to the public or to any other category of investors.

Pricing

The qualified institutions placement is required to be made at a price not less than the average of the weekly high and low of the closing prices of the equity shares of the same class listed on the stock exchange during the two weeks preceding the relevant date.

However, the issuer may offer a discount of not more than five per cent on the price so calculated for the qualified institutions placement, subject to approval of shareholders.

If the eligible securities are convertible into or exchangeable with equity shares, the issuer is required to determine the price of such equity shares allotted pursuant to such conversion or exchange taking the relevant date as decided and disclosed by it while passing the special resolution.

Issue of partly paid up securities

The issuer can not allot partly paid up securities. In case of allotment of equity shares on exercise of options attached to warrants, such equity shares shall be fully paid up. However, on allotment of non convertible debt instruments along with warrants, the allottees can pay the full consideration or part thereof payable with respect to warrants, at the time of allotment of such warrants.

The prices determined for qualified institutions placement are subject to appropriate adjustments in certain cases. If the issuer :

- makes an issue of equity shares by way of capitalization of profits or reserves, other than by way of a dividend on shares.
- makes a rights issue of equity shares.
- consolidates its outstanding equity shares into a smaller number of shares.
- divides its outstanding equity shares including by way of stock split.
- re-classifies any of its equity shares into other securities of the issuer.
- is involved in such other similar events or circumstances, which in the opinion of the concerned stock exchange, requires adjustments.

Here stock exchange means any of the recognised stock exchanges in which the equity shares of the same class of the issuer are listed and in which the highest trading volume in such equity shares has been recorded during the two weeks immediately preceding the relevant date.

Restrictions on allotment

- Minimum 10% of eligible securities is required to be allotted to mutual funds. In case the mutual funds do not subscribe to said minimum percentage or any part thereof, such minimum portion or part thereof can be allotted to other qualified institutional buyers.
- An allotment can not be made, either directly or indirectly, to any qualified institutional buyer who is a promoter or any person related to promoters of the issuer.
- A qualified institutional buyer who does not hold any shares in the issuer and who has acquired the said rights in the capacity of a lender can not be deemed to be a person related to promoters.
- In a qualified institutions placement of non-convertible debt instrument along with warrants, an investor can subscribe to the combined offering of non-convertible debt instruments with warrants or to the individual securities, that is, either non- convertible debt instruments or warrants.

Here a qualified institutional buyer who has any of the following rights is deemed to be a person related to the promoters of the issuer:

- (a) rights under a shareholders' agreement or voting agreement entered into with promoters or persons related to the promoters.
- (b) veto rights or
- (c) right to appoint any nominee director on the board of the issuer.

Do you know?

The application in qualified institutions placement can not withdraw their bids after the closure of the issue.

Minimum numbers of allottees

- If the size of the issue is less than of equal to 250 crore rupees minimum two allottees for each placement and where the issue size is greater than 250 rupees minimum of five allottees required.
- A single allottee can not be allotted more than 50% of the issue size.

- The qualified institutional buyers belonging to the same group or who are under same control are deemed to be a single allottee.

Validity of the special resolution

An allotment pursuant to the special resolution approving the proposed QIP is required to be completed within a period of twelve months from the date of passing of the resolution.

The issuer can not make subsequent qualified institutions placement until expiry of six months from the date of the prior qualified institutions placement made pursuant to one or more special resolutions.

Do you know ?

Allotment to QIBs is to be made within 12 months of passing Special Resolution approving such allotment.

Restriction on amount raised

The aggregate of the proposed QIP and all previous QIPs made by the issuer in the same financial year should not exceed five times the net worth of the issuer as per the audited balance sheet of the previous financial year.

Tenure

The tenure of the convertible or exchangeable eligible securities issued through qualified institutions placement should not be more than sixty months from the date of allotment.

Transferability of Securities

The eligible securities allotted can not be sold by the allottee for a period of one year from the date of allotment, except on a recognised stock exchange.

INSTITUTIONAL PLACEMENT PROGRAMME

“Institutional Placement Programme” means a further public offer of eligible securities by an eligible seller, in which the offer, allocation and allotment of such securities is made only to qualified institutional buyers in terms of this Chapter.

SEBI vide its notification dated January 30, 2012 has amended the Issue of Capital and Disclosure Requirements Regulations, 2009 whereby Chapter VIII-A - Institutional Placement Programme (IPP) has been inserted.

The provisions of this Chapter shall apply to issuance of fresh shares and/or offer for sale of shares in a listed issuer for the purpose of achieving minimum public shareholding in terms of Rule 19(2)(b) and 19A of the Securities Contracts (Regulation) Rules, 1957.

Conditions for Institutional Placement Programme

- An institutional placement programme may be made only after a special resolution approving the institutional placement programme has been passed by the shareholders of the issuer in terms of section 62 of the Companies Act, 2013.
- No partly paid-up securities shall be offered.
- The issuer shall obtain an in-principle approval from the stock exchange(s).

Appointment of Merchant Banker

An institutional placement programme shall be managed by merchant banker(s) registered with the SEBI who shall exercise due diligence.

Offer Document

- The institutional placement programme shall be made on the basis of the offer document which shall contain all material information.

- The issuer shall, simultaneously while registering the offer document with the Registrar of Companies, file a copy thereof with SEBI and with the stock exchange(s) through the lead merchant banker.
- The issuer shall file the soft copy of the offer document with SEBI, along with the fee.
- The offer document shall also be placed on the website of the concerned stock exchange and of the issuer clearly stating that it is in connection with institutional placement programme and that the offer is being made only to the qualified institutional buyers.
- The merchant banker shall submit to SEBI a due diligence certificate, stating that the eligible securities are being issued under institutional placement programme and that the issuer complies with requirements of this Chapter.

Pricing and Allocation/allotment

- The eligible seller shall announce a floor price or price band at least one day prior to the opening of institutional placement programme.
- The eligible seller shall have the option to make allocation/allotment as per any of the following methods –
 - (a) proportionate basis;
 - (b) price priority basis; or
 - (c) criteria as mentioned in the offer document.
- The method chosen shall be disclosed in the offer document.
- Allocation/allotment shall be overseen by stock exchange before final allotment.

Restrictions

The promoter or promoter group shall not make institutional placement programme if the promoter or any person who is part of the promoter group has purchased or sold the eligible securities during the 12 weeks period prior to the date of the programme and they shall not purchase or sell the eligible securities during the twelve weeks period after the date of the programme.

However, such promoter or promoter group may, within the period provided above, offer eligible securities held by them through institutional placement programme or offer for sale through stock exchange mechanism specified by SEBI, subject to the condition that there shall be a gap of minimum two weeks between the two successive offer(s) and /or programme(s).

- Allocation/allotment under the institutional placement programme shall be made subject to the following conditions:
 - (a) Minimum of twenty five per cent of eligible securities shall be allotted to mutual funds and insurance companies. However, if the mutual funds and insurance companies do not subscribe to said minimum percentage or any part thereof, such minimum portion or part thereof may be allotted to other qualified institutional buyers;
 - (b) No allocation/allotment shall be made, either directly or indirectly, to any qualified institutional buyer who is a promoter or any person related to promoters of the issuer. However, a qualified institutional buyer who does not hold any shares in the issuer and who has acquired the rights in the capacity of a lender shall not be deemed to be a person related to promoters.
- The issuer shall accept bids using ASBA facility only.
- The bids made by the applicants in institutional placement programme shall not be revised downwards or withdrawn.

Minimum number of allottees

The minimum number of allottees for each offer of eligible securities made under institutional placement

programme shall not be less than ten. However, no single allottees shall be allotted more than twenty five per cent of the offer size.

The QIBs belonging to the same group or who are under same control shall be deemed to be a single allottee.

Restrictions on size of the offer

- The aggregate of all the tranches of institutional placement programme made by the eligible seller shall not result in increase in public shareholding by more than ten per cent or such lesser per cent as is required to reach minimum public shareholding.
- Where the issue has been oversubscribed, an allotment of not more than ten percent of the offer size shall be made by the eligible seller.

Period of Subscription and display of demand

- The issue shall be kept open for a minimum of one day or maximum of two days.
- The aggregate demand schedule shall be displayed by stock exchange(s) without disclosing the price.

Withdrawal of offer

The eligible seller shall have the right to withdraw the offer in case it is not fully subscribed.

Transferability of eligible securities

The eligible securities allotted under institutional placement programme shall not be sold by the allottee for a period of one year from the date of allocation/allotment, except on a recognised stock exchange.

LISTING ON INSTITUTIONAL TRADING PLATFORM

Applicability

These provisions shall apply to entities which seek listing of their securities exclusively on the ITP either pursuant to a public issue or otherwise.

Provisions of SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009 that shall not apply to such entities :

1. Provisions relating to minimum public shareholding would not be applicable to entities listed on institutional trading platform without making a public issue.
2. A cap on the money spent by companies on publicity and advertisements as start-ups need to spend much more for such purposes.

Accessibility of ITP

ITP shall be accessible to institutional investors as well as non-institutional investors.

(a) “**Institutional Trading Platform**” means the trading platform for listing and trading of specified securities of entities that comply with the eligibility criteria specified in these regulation.

(b) “**Institutional Investor**” means qualified institutional buyer or family trust or systematically important NBFCs registered with RBI or intermediaries registered with SEBI, all with net-worth of more than 500 crore rupees, as per the last audited financial statements.

(i) Eligibility

The following entities eligible for listing on the institutional trading platform:-

- an entity which is intensive in the use of technology, information technology, intellectual property, data analytics, bio-technology or nano technology to provide products, services or business platforms with substantial value addition and at least 25% of its pre-issue capital is held by qualified institutional buyer(s)

as on the date of filing of draft information document or draft offer document with SEBI, as the case may be; or

- any other entity in which at least 15% of the pre-issue capital is held by qualified institutional buyers as on the date of filing of draft information document or draft offer document with SEBI, as the case may be.

No person, individually or collectively with persons acting in concert, shall hold 25% or more of the post-issue share capital in such entity.

(ii) Listing without public issue

- An entity seeking listing of its specified securities without making a public issue shall file a draft information document along with necessary documents with SEBI in accordance with these regulations along with fee as specified in the regulations. The draft information document shall contain the disclosures as specified for draft offer document in these regulations.

However, the following shall not be applicable in case of listing without public issue:

- (i) Allotment
- (ii) Issue opening / closing;
- (iii) Advertisement;
- (iv) Underwriting;
- (v) Regulation 26(5)
- (vi) Pricing;
- (vii) Dispatch of issue material; and
- (viii) Other such provisions related to offer of specified securities to public.
- The entity shall obtain in-principle approval from the recognised stock exchanges on which it proposes to get its specified securities listed and list its specified securities on the recognised stock exchange(s) within 30 days from the date of issuance of observations by SEBI or from the expiry of the period if SEBI has not issued any such observations.
- The entity which has received in-principle approval from the recognised stock exchange for listing of its specified securities on the institutional trading platform, without making a public issue, shall be deemed to have been waived by SEBI under Rule 19(7) from the requirement of Rule 19(2) (b) of Securities Contracts (Regulation) Rules, 1957 for the limited purpose of listing on the institutional trading platform.
- Provisions relating to minimum public shareholding shall not apply to entities listed on institutional trading platform without making a public issue.
- The draft and final information document shall be approved by the board of directors of the entity and shall be signed by all directors, the Chief Executive Officer, i.e., the Managing Director or Manager within the meaning of the Companies Act, 2013 and the Chief Financial Officer, i.e., the Whole-time Finance Director or any other person heading the finance function and discharging that function.
- The signatories shall also certify that all disclosures made in the information document are true and correct.
- In case of mis-statement in the information document or any omission therein, any person who has authorized the issue of information document shall be liable in accordance with the provisions of the SEBI Act, 1992 and regulations made there under.

(iii) Listing pursuant to public issue

- An entity seeking issue and listing of its specified securities shall file a draft offer document along with necessary documents with SEBI in accordance with these regulations along with fees as specified in the regulations.

- The minimum application size shall be 10 lakh rupees.
- The number of allottees shall be more than 200.
- The allocation in the net offer to public category shall be as follows:
 - (a) 75 % to institutional investors, there shall be no separate allocation for Anchor Investors
 - (b) 25 % to non-institutional investors;
- Any under-subscription in the non-institutional investor category shall be available for subscription under the institutional investors' category.
- The allotment to institutional investors may be on a discretionary basis, no institutional investor shall be allotted more than 10% of the issue size. Whereas the allotment to non-institutional investors shall be on a proportionate basis.
- The mode of allotment to institutional investors, i.e., whether discretionary or proportionate, shall be disclosed prior to or at the time of filing of the Red Herring Prospectus.
- In case of discretionary allotment to institutional investors, no institutional investor shall be allotted more than 10% of the issue size.
- The offer document shall disclose the broad objects of the issue.
- The basis of issue price may include disclosures, except projections, as deemed fit by the issuers in order to enable investors to take informed decisions and the disclosures shall suitably caution the investors about basis of valuation.

(iv) Lock-in

1. The entire pre-issue capital of the shareholders shall be locked-in for a period of six months from the date of allotment in case of listing pursuant to public issue or date of listing in case of listing without public issue.

However, this regulation shall not apply to:-

- (i) equity shares allotted to employees under an employee stock option or employee stock purchase scheme of the entity prior to the initial public offer, if the entity has made full disclosures with respect to such options or scheme;
- (ii) equity shares held by a venture capital fund or alternative investment fund of Category I or a foreign venture capital investor;

However, such equity shares shall be locked in for a period of at least one year from the date of purchase by the venture capital fund or alternative investment fund or foreign venture capital investor.

- (iii) equity shares held by persons other than promoters, continuously for a period of at least one year prior to the date of listing in case of listing without public issue

Explanation.- For the purpose of clause (ii) and (iii), 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 the convertible securities shall be deemed to be fully paid-up, if the entire consideration payable thereon has been paid at the time of their conversion.

2. The 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 if the pledge of specified securities is one of the terms of sanction of the loan.
3. The specified securities that are locked-in may be transferable in accordance with these regulations.
4. All specified securities allotted on a discretionary basis shall be locked-in in accordance with the

requirements for lock-in by Anchor Investors on main board of the stock exchange, as specified under clause 10(j) in Part A of Schedule XI.

(v) Trading lot

The minimum trading lot shall be ten lakh rupees.

(vi) Exit of entities listed without making a public issue

- An entity whose specified securities are listed on the institutional trading platform without making a public issue may exit from that platform, if-
 - (a) its shareholders approve such exit by passing a special resolution through postal ballot where 90% of the total votes and the majority of non-promoter votes have been cast in favour of such proposal; and
 - (b) the recognised stock exchange where its shares are listed approve of such an exit.
- The recognised stock exchange may delist the specified securities of an entity listed without making a public issue upon non-compliance of the conditions of listing and in the manner as specified by the stock exchange.
- No entity promoted by promoters and directors of an entity delisted, shall be permitted to list on institutional trading platform for a period of five years from the date of such delisting.

However, the provisions of this regulation shall not apply to another entity promoted by the independent directors of such a delisted entity.

(vii) Migration to Main Board

An entity that has listed its specified securities on a recognised stock exchange in accordance with the provisions of this Chapter may at its option migrate to the main board of that recognised stock exchange after expiry of three years from the date of listing subject to compliance with the eligibility requirements of the stock exchange.

ISSUE OF SECURITIES BY SMALL AND MEDIUM ENTERPRISES

The necessary provisions for the listing of specified securities under the SME Platform have been made in accordance with the Chapter XB of Issue of Capital and Disclosure Requirements (ICDR).

APPLICABILITY

A company can issue specified securities if :

- The post-issue face value capital does not exceed 10 crore rupees.
- The post issue face value capital is more than 10 crore rupees and upto 25 crore rupees.

FILING OF OFFER DOCUMENT

A company is not required to file the draft offer document with SEBI as in case of public issue. But the company has to file a copy of the offer document with SEBI through a merchant banker, simultaneously with the filing of the prospectus with the SME exchange and the Registrar of Companies or letter of offer with the SME Exchange. SEBI should not issue any observation on the offer document.

The offer document shall be displayed from the date of filing on the websites of SEBI, the issuer, the merchant banker and the SME exchange where the specified securities offered through the offer document are proposed to be listed.

MINIMUM APPLICATION VALUE AND NUMBER OF ALLOTTEES

- The minimum application size in terms of number of specified securities shall not be less than one lakh rupees per application.
- The minimum number of prospective allottees should be less than fifty.

LISTING OF SPECIFIED SECURITIES

- The specified securities issue in accordance with the provision of SEBI ICDR regulations will be listed on SME exchange.
- A listed company can migrate the specified securities already listed on any recognized stock exchange/s to the SME exchange.

MIGRATION TO SME EXCHANGE

A listed company whose post-issue face value capital is less than 25 crore rupees can migrate its specified securities to SME exchange –

- if its shareholders approve such migration by passing a special resolution through postal ballot to this effect and
- if such issuer fulfils the eligibility criteria for listing laid down by the SME exchange.

However, the special resolution shall be acted upon if and only if the votes cast by shareholders other than promoters in favour of the proposal amount to at least two times the number of votes cast by shareholders other than promoter shareholders against the proposal.

MIGRATION TO MAIN BOARD

- An company, whose specified securities are listed on a SME Exchange and whose post issue face value capital is more than 10 crore rupees and upto 25 crore rupees, can migrate its specified securities to Main Board –
 - if its shareholders approve such migration by passing a special resolution through postal ballot to this effect and
 - if such issuer fulfils the eligibility criteria for listing laid down by the Main Board.

However, the special resolution shall be acted upon if and only if the votes cast by shareholders other than promoters in favour of the proposal amount to at least two times the number of votes cast by shareholders other than promoter shareholders against the proposal.

- Where the post issue face value capital of an issuer listed on SME exchange is likely to increase beyond 25 crore rupees by virtue of any further issue of capital by the issuer by way of rights issue, preferential issue, bonus issue, etc. the issuer shall migrate its specified securities listed on SME exchange to Main Board and seek listing of specified securities proposed to be issued on the Main Board subject to the fulfilment of the eligibility criteria for listing of specified securities laid down by the Main Board.

However, no further issue of capital by the issuer shall be made unless –

- (a) the shareholders of the issuer have approved the migration by passing a special resolution through postal ballot wherein the votes cast by shareholders other than promoters in favour of the proposal amount to at least two times the number of votes cast by shareholders other than promoter shareholders against the proposal.
- (b) the issuer has obtained in- principle approval from the Main Board for listing of its entire specified securities on it.

UNDERWRITING OBLIGATION

- The issue shall be 100 % underwritten.
- The merchant banker/s shall underwrite at least fifteen per cent of the issue size on his/ their own account/s.

- The issuer in consultation with merchant banker may appoint underwriters and the merchant banker may enter into an agreement with nominated investor indicating therein the number of specified securities which they agree to subscribe at issue price in case of under-subscription.
- If other underwriters fail to fulfill their underwriting obligations or other nominated investors fail to subscribe to unsubscribed portion, the merchant banker shall fulfill the underwriting obligations.
- The underwriters other than the merchant banker and the nominated investors, who have entered into an agreement for subscribing to the issue in case of under-subscription, shall not subscribe to the issue in any manner except for fulfilling their obligations under their respective agreements with the merchant banker in this regard.
- All the underwriting and subscription arrangements made by the merchant banker shall be disclosed in the offer document.
- The merchant banker shall file an undertaking to SEBI that the issue has been 100 % underwritten along with the list of underwriters and nominated investors indicating the extent of underwriting or subscription commitment made by them, one day before the opening of issue.

MARKET MAKING

- The merchant banker ensure that there shall be compulsory market making through the stock brokers of SME exchange for a minimum period of three years from the date of listing of specified securities.
- The merchant banker may enter into agreement with nominated investors for receiving or delivering the specified securities in the market making subject to the prior approval by the SME exchange where the specified securities are proposed to be listed.
- The company shall disclose the details of arrangement of market making in the offer document.
- The specified securities being bought or sold in the process of market making may be transferred to or from the nominated investor with whom the merchant banker has entered into an agreement for the market making. However, the inventory of the market maker, as on the date of allotment of the specified securities, shall be at least 5 % of the specified securities proposed to be listed on SME exchange.
- The market maker shall buy the entire shareholding of a shareholder of the issuer in one lot, where value of such shareholding is less than the minimum contract size allowed for trading on the SME exchange. However, the market maker shall not sell in lots less than the minimum contract size allowed for trading on the SME exchange.
- Market maker shall not buy the shares from the promoters or persons belonging to promoter group of the issuer or any person who has acquired shares from such promoter or person belonging to promoter group, during the compulsory market making period.
- The promoters' holding shall not be eligible for offering to the market maker. However, the promoters' holding which is not locked-in as per these regulations can be traded with prior permission of the SME exchange.
- Subject to the agreement between the issuer and the merchant banker/s, the merchant banker/s who have the responsibility of market making may be represented on the board of the issuer.

Term one should Know

Main Board

It means a recognized stock exchange having nationwide trading terminals, other than SME exchange.

Nominated investor

It means a qualified institutional buyer or private equity fund, who enters into an agreement with the merchant banker to subscribe to the issue in case of under-subscription or to receive or deliver the specified securities in the market making process.

LISTING OF SECURITIES ON STOCK EXCHANGES**IN-PRINCIPLE APPROVAL OF RECOGNIZED STOCK EXCHANGE(S)**

Regulation 107 stipulates that the issuer or the issuing company, as the case may be, shall obtain in-principle approval from recognised stock exchange as follows:

- (a) In case of an initial public offer (IPO) or an issue of Indian Depository Receipts (IDR), from all the recognised stock exchange(s) on which the issuer or the issuing company, proposes to get its specified securities or IDRs, as the case may be, listed and
- (b) In case of other issues, before issuance of further securities, as follows:
 - where the securities are listed only on recognised stock exchange(s) having nationwide trading terminals, from all such stock exchange(s);
 - where the securities are not listed on any recognised stock exchange having nationwide trading terminals, from all the stock exchange(s) on which the securities of the issuer are proposed to be listed;
 - where the securities are listed on recognised stock exchange(s) having nationwide trading terminals as well as on the recognised stock exchange(s) not having nationwide trading terminals, from all recognised stock exchange(s) having nationwide trading terminals.

APPLICATION FOR LISTING

The issuer or the issuing company, as the case may be, shall complete the prelisting formalities within the time specified by SEBI. The issuer or the issuing company, as the case may be, shall make an application for listing, within twenty days from the date of allotment, to one or more recognized stock exchange(s) along with the documents specified by stock exchange(s).

In case of delay in making application for listing beyond twenty days from the date of allotment, the issuer or the issuing company, as the case may be, shall pay penal interest at the rate of at least 10% per annum to allottees for each day of delay from the expiry of thirty days from date of allotment till the listing of such securities to the allottees. In the event of non-receipt of listing permission from the stock exchange(s) by the issuer or the issuing company, as the case may be, or withdrawal of observation letter issued by SEBI, wherever applicable, the securities shall not be eligible for listing and the issuer or the issuing company, as the case may be, shall be liable to refund the subscription monies, if any, to the respective allottees immediately along with interest at the rate of 10% per annum from the date of allotment.

LISTING AGREEMENT

The issuer or the issuing company desirous of listing its securities on a recognised stock exchange shall execute a listing agreement with stock exchange. The issuer or the issuing company who has previously entered into agreement(s) with a recognised stock exchange to list its securities shall execute a fresh listing agreement with such stock exchange within six months of the date of notification of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015.

OBLIGATION OF STOCK EXCHANGE(s)

The stock exchange(s) shall grant in-principle approval/list the securities or reject the application for in-principle approval /listing by the issuer or issuing company, as the case may be, within thirty days from the later of the date of receipt of application for in-principle approval/listing from issuer or the issuing company, as the case may be, or the date of receipt of satisfactory reply from the issuer or the issuing company, as the case maybe, in cases where the stock exchange(s) has sought any clarification from them.

EXIT OPPORTUNITY TO DISSENTING SHAREHOLDERS

SEBI vide its circular dated on February 17, 2016 amended the SEBI (ICDR) Regulations, 2009 and inserted Chapter VI-A-**‘Conditions and Manner of Providing Exit Opportunity to Dissenting Shareholders.’**

The provisions of this Chapter shall apply to an exit offer made by the promoters or shareholders in control of an issuer to the dissenting shareholders in terms of section 13(8) and section 27(2) of the Companies Act, 2013, in case of change in objects or variation in the terms of contract referred to in the prospectus.

Who is Dissenting Shareholders?

“Dissenting Shareholders” mean those shareholders who have voted against the resolution for change in objects or variation in terms of a contract, referred to in the prospectus of the issuer;

However, the provisions of this Chapter shall not apply where there are neither identifiable promoters nor shareholders in control of the listed issuer.

CONDITIONS FOR EXIT OFFER

The promoters or shareholders in control shall make the exit offer in accordance with the provisions of this Chapter, to the dissenting shareholders, if:

- the public issue has opened after April 1, 2014; and
- the proposal for change in objects or variation in terms of a contract, referred to in the prospectus is dissented by at least 10 per cent of the shareholders who voted in the general meeting; and
- the amount to be utilized for the objects for which the prospectus was issued is less than 75 % of the amount raised (including the amount earmarked for general corporate purposes as disclosed in the offer document).

ELIGIBILITY OF SHAREHOLDERS FOR AVAILING THE EXIT OFFER

Regulation 69D of SEBI (ICDR) Regulations, 2009 provides that only those dissenting shareholders of the issuer who are holding shares as on the relevant date shall be eligible to avail the exit offer.

EXIT OFFER PRICE

The ‘exit price’ payable to the dissenting shareholders shall be the highest of the following:

- (a) the volume weighted average price paid or payable for acquisitions, whether by the promoters or shareholders having control or by any person acting in concert with them, during the fifty two weeks immediately preceding the relevant date;
- (b) the highest price paid or payable for any acquisition, whether by the promoters or shareholders having control or by any person acting in concert with them, during the twenty six weeks immediately preceding the relevant date;
- (c) the volume weighted average market price of such shares for a period of sixty trading days immediately preceding the relevant date as traded on the recognised stock exchange where the maximum volume

of trading in the shares of the issuer are recorded during such period, provided such shares are frequently traded;

- (d) where the shares are not frequently traded, the price determined by the promoters or shareholders having control and the merchant banker taking into account valuation parameters including book value, comparable trading multiples, and such other parameters as are customary for valuation of shares of such issuers.

MANNER OF PROVIDING EXIT TO DISSENTING SHAREHOLDERS

- The notice proposing the passing of special resolution for changing the objects of the issue and varying the terms of contract, referred to in the prospectus shall also contain information about the exit offer to the dissenting shareholders.
- In addition to the disclosures required under the provisions of section 102 of the Companies Act, 2013 read with rule 32 of the Companies (Incorporation) Rules, 2014 and rule 7 of the Companies (Prospectus and Allotment of Securities) Rules, 2014 and any other applicable law, a statement to the effect that the promoters or the shareholders having control shall provide an exit opportunity to the dissenting shareholders shall also be included in the explanatory statement to the notice for passing special resolution.
- After passing of the special resolution, the issuer shall submit the voting results to the recognised stock exchange(s), in terms of the provisions of regulation 44(3) of SEBI (LODR) Regulations, 2015.
- The issuer shall also submit the list of dissenting shareholders, as certified by its compliance officer, to the recognised stock exchange(s).
- The promoters or shareholders in control, shall appoint a merchant banker registered with SEBI and finalize the exit offer price in accordance with these regulations.
- The issuer shall intimate the recognised stock exchange(s) about the exit offer to dissenting shareholders and the price at which such offer is being given.
- The recognised stock exchange(s) shall immediately on receipt of such intimation disseminate the same to public within one working day.
- To ensure security for performance of their obligations, the promoters or shareholders having control, as applicable, shall create an escrow account which may be interest bearing and deposit the aggregate consideration in the account at least two working days prior to opening of the tendering period.
- The tendering period shall start not later than seven working days from the passing of the special resolution and shall remain open for ten working days.
- The dissenting shareholders who have tendered their shares in acceptance of the exit offer shall have the option to withdraw such acceptance till the date of closure of the tendering period.
- The promoters or shareholders having control shall facilitate tendering of shares by the shareholders and settlement of the same through the recognised stock exchange mechanism as specified by SEBI for the purpose of takeover, buy-back and delisting.
- The promoters or shareholders having control shall, within a period of ten working days from the last date of the tendering period, make payment of consideration to the dissenting shareholders who have accepted the exit offer.
- Within a period of two working days from the payment of consideration, the issuer shall furnish to the recognised stock exchange(s), disclosures giving details of aggregate number of shares tendered, accepted, payment of consideration and the post-offer shareholding pattern of the issuer and a report by the merchant banker that the payment has been duly made to all the dissenting shareholders whose shares have been accepted in the exit offer.

MAXIMUM PERMISSIBLE NON-PUBLIC SHAREHOLDING

Regulation 69G of SEBI (ICDR) Regulations, 2009 provides that, in the event, the shares accepted in the exit offer were such that the shareholding of the promoters or shareholders in control, taken together with persons acting in concert with them pursuant to completion of the exit offer results in their shareholding exceeding the maximum permissible non-public shareholding, the promoters or shareholders in control, as applicable, shall be required to bring down the non-public shareholding to the level specified and within the time permitted under Securities Contract (Regulation) Rules, 1957.

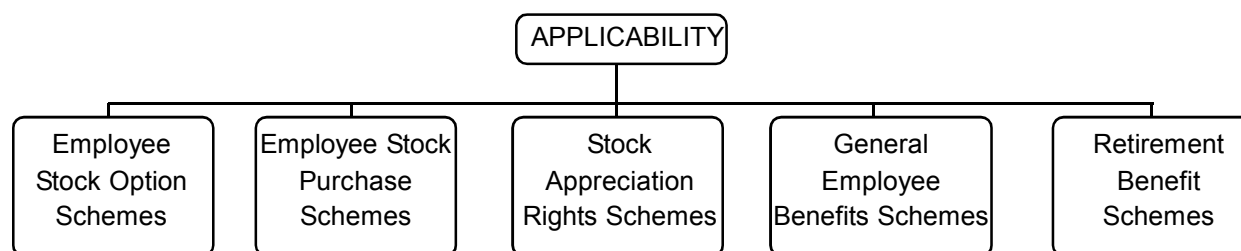
SEBI (SHARE BASED EMPLOYEE BENEFITS) REGULATIONS, 2014

SEBI has, on 28th October 2014 notified SEBI (Share Based Employee Benefits) Regulations, 2014 to provide for regulation of all schemes by companies for the benefit of their employees involving dealing in shares, directly or indirectly, with a view to facilitate smooth operation of such schemes while preventing any possible manipulation and matters connected therewith or incidental thereto.

The SEBI (Share Based Employee Benefits) Regulations, 2014 comprises of four chapters. Chapter I deal mainly with the preliminary and definition used in regulation. Chapter II provides for implementation and process of scheme. Chapter III deals with administration of specific schemes. Chapter IV deals with miscellaneous provisions.

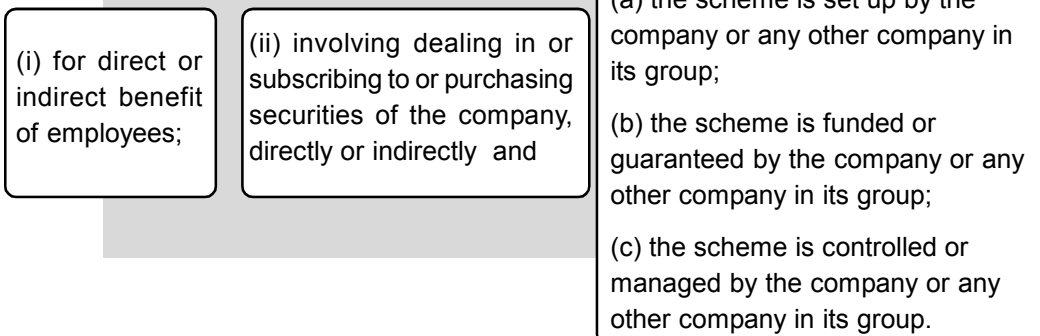
APPLICABILITY

The provisions of these regulations shall apply to following:-



COMPANIES COVERED

The provisions of these regulations shall apply to any company whose shares are listed on a recognised stock exchange in India, and has a scheme:



NON- APPLICABILITY

- These regulations shall not apply to shares issued to employees in compliance with the provisions pertaining to preferential allotment as specified in the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009.
- The provisions pertaining to preferential allotment as specified in SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009 shall not be applicable in case of a company issuing new shares in pursuance and compliance of these regulations.

IMPORTANT DEFINITIONS

“Appreciation” means the difference between the market price of the share of a company on the date of exercise of stock appreciation right (SAR) or vesting of SAR, as the case may be, and the SAR price.

“Employee Stock Option Scheme” means a scheme under which a company grants employee stock option directly or through a trust.

“Employee Stock Purchase Scheme” means a scheme under which a company offers shares to employees, as part of public issue or otherwise, or through a trust where the trust may undertake secondary acquisition for the purposes of the scheme.

“General Employee Benefits Scheme” means any scheme of a company framed in accordance with these regulations, dealing in shares of the company or the shares of its listed holding company, for the purpose of employee welfare including healthcare benefits, hospital care or benefits, or benefits in the event of sickness, accident, disability, death or scholarship funds, or such other benefit as specified by such company.

“Relevant Date” means,-

- (i) in the case of grant, the date of the meeting of the compensation committee on which the grant is made; or
- (ii) in the case of exercise, the date on which the notice of exercise is given to the company or to the trust by the employee;

“Retirement Benefit Scheme” means a scheme of a company, framed in accordance with these regulations, dealing in shares of the company or the shares of its listed holding company, for providing retirement benefits to the employees subject to compliance with existing rules and regulations as applicable under laws relevant to retirement benefits in India.

“Stock Appreciation Right” means a right given to a SAR grantee entitling him to receive appreciation for a specified number of shares of the company where the settlement of such appreciation may be made by way of cash payment or shares of the company.

Explanation - An SAR settled by way of shares of the company shall be referred to as equity settled SAR.

“Stock Appreciation Right Scheme” means a scheme under which a company grants SAR to employees.

SCHEMES - IMPLEMENTATION AND PROCESS**IMPLEMENTATION OF SCHEMES THROUGH TRUST**

1. A company may implement schemes either :-
 - a) directly or
 - b) by setting up an irrevocable trust(s)

However, if the scheme is to be implemented through a trust the same has to be decided upfront at the time of taking approval of the shareholders for setting up the schemes.

However, if the scheme involves secondary acquisition or gift or both, then it is mandatory for the company to implement such scheme(s) through a trust(s).

2. A company may implement several schemes as permitted under these regulations through a single trust.

However, such single trust shall keep and maintain-

- proper books of account,
- records and documents,

for each such scheme so as to explain its transactions and to disclose at any point of time the financial position of each scheme and in particular give a true and fair view of the state of affairs of each scheme.

3. SEBI may specify the minimum provisions to be included in the trust deed under which the trust is formed, and such trust deed and any modifications thereto shall be mandatorily filed with the stock exchange in India where the shares of the company are listed.
4. A person shall not be appointed as a trustee, if he-
 - (i) is a director, key managerial personnel or promoter of the company or its holding, subsidiary or associate company or any relative of such director, key managerial personnel or promoter; or
 - (ii) beneficially holds ten percent or more of the paid-up share capital of the company;

However, where individuals or 'one person companies' as defined under the Companies Act, 2013 are appointed as trustees, there shall be a minimum of two such trustees, and in case a corporate entity is appointed as a trustee, then it may be the sole trustee.

5. The trustees of a trust, which is governed under these regulations, shall not vote in respect of the shares held by such trust, so as to avoid any misuse arising out of exercising such voting rights.
6. The trustee should ensure that appropriate approval from the shareholders has been obtained by the company in order to enable the trust to implement the scheme(s) and undertake secondary acquisition for the purposes of the scheme(s).
7. The trust shall not deal in derivatives, and shall undertake only delivery based transactions for the purposes of secondary acquisition as permitted by these regulations.
8. The company may lend monies to the trust on appropriate terms and conditions to acquire the shares either through new issue or secondary acquisition, for the purposes of implementation of the scheme(s).
9. For the purposes of disclosures to the stock exchange, the shareholding of the trust shall be shown as 'non-promoter and non-public' shareholding.

Explanation: For the removal of doubts, it is clarified that shares held by the trust shall not form part of the public shareholding which needs to be maintained at a minimum of twenty five per cent as prescribed under Securities Contracts (Regulation) Rules, 1957

10. Secondary acquisition in a financial year by the trust shall not exceed two per cent of the paid up equity capital as at the end of the previous financial year.
11. The total number of shares under secondary acquisition held by the trust shall at no time exceed the below mentioned prescribed limits as a percentage of the paid up equity capital as at the end of the

financial year immediately prior to the year in which the shareholder approval is obtained for such secondary acquisition:

Sr. No.	Particulars	Limit
A	for the schemes enumerated in Part A, Part B or Part C of Chapter III of these regulations	5%
B	for the schemes enumerated in Part D, or Part E of Chapter III of these regulations	2%
C	for all the schemes in aggregate	5%

12. The un-appropriated inventory of shares which are not backed by grants, acquired through secondary acquisition by the trust under Part A, Part B or Part C of these regulations, shall be appropriated within a reasonable period which shall not extend beyond the end of the subsequent financial year.

However, if such trust(s) existing as on the date of notification of these regulations are not able to appropriate the un-appropriated inventory within one year of such notification, the same shall be disclosed to the stock exchange(s) at the end of such period and then the same shall be sold on the recognized stock exchange(s) where shares of the company are listed, within a period of five years from the date of notification of these regulations.

13. The trust shall be required to hold the shares acquired through secondary acquisition for a minimum period of six months except where they are required to be transferred in the circumstances enumerated in this regulation, whether off market or on the platform of stock exchange.

14. The trust shall be permitted to undertake off-market transfer of shares only under the following circumstances:

- transfer to the employees pursuant to scheme(s);
- when participating in open offer under SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011, or when participating in buy-back, delisting or any other exit offered by the company generally to its shareholders.

15. The trust shall not become a mechanism for trading in shares and hence shall not sell the shares in secondary market except under the following circumstances:

- cashless exercise of options under the scheme as prescribed in these regulations;
- on vesting or exercise, as the case may be, of SAR under the scheme as prescribed in these regulations;
- in case of emergency for implementing the schemes covered under Part D and Part E of Chapter III of these regulations, and for this purpose -
 - the trustee shall record the reasons for such sale; and
 - money so realised on sale of shares shall be utilised within a definite time period as stipulated under the scheme or trust deed.
- participation in buy-back or open offers or delisting offers or any other exit offered by the company generally to its shareholders, if required;
- for repaying the loan, if the un-appropriated inventory of shares held by the trust is not appropriated within the timeline as provided above.
- winding up of the scheme(s); and

- g) based on approval granted by SEBI to an applicant, for the reasons recorded in writing in respect of the schemes covered in these regulations, upon payment of a non-refundable fee of rupees one lakh along with the application by way of direct credit in the bank account through NEFT/RTGS/IMPS or any other mode allowed by RBI or by way of a banker's cheque or demand draft payable at Mumbai in favour of SEBI.
16. The trust shall be required to make disclosures and comply with the other requirements applicable to insiders or promoters under the SEBI (Prohibition of Insider Trading) Regulations, 2015 or any modification or re-enactment thereto.

ELIGIBILITY CRITERIA

An employee shall be eligible to participate in the schemes of the company as determined by the compensation committee.

Explanation-

Where such employee is a director nominated by an institution as its representative on the board of directors of the company –

- (i) *The contract or agreement entered into between the institution nominating its employee as the director of a company, and the director so appointed shall, inter alia, specify the following:-*
 - (a) whether the grants by the company under its scheme(s) can be accepted by the said employee in his capacity as director of the company;
 - (b) that grant if made to the director, shall not be renounced in favour of the nominating institution; and
 - (c) the conditions subject to which fees, commissions, other incentives, etc. can be accepted by the director from the company.
- (ii) *The institution nominating its employee as a director of a company shall file a copy of the contract or agreement with the said company, which shall, in turn file the copy with all the stock exchanges on which its shares are listed.*
- (iii) *The director so appointed shall furnish a copy of the contract or agreement at the first board meeting of the company attended by him after his nomination.*

COMPENSATION COMMITTEE

- A company shall constitute a compensation committee for administration and superintendence of the schemes.

However, the company may designate such of its other committees as compensation committee if they fulfil the criteria as prescribed in these regulations. Further that where the scheme is being implemented through a trust the compensation committee shall delegate the administration of such scheme(s) to the trust.

- The compensation committee shall be a committee of such members of the board of directors of the company as provided under section 178 of the Companies Act, 2013, as amended or modified from time to time.
- The compensation committee shall, *inter alia*, formulate the detailed terms and conditions of the schemes which shall include the provisions as specified by SEBI in this regard.
- The compensation committee shall frame suitable policies and procedures to ensure that there is no

violation of securities laws, as amended from time to time, including SEBI (Prohibition of Insider Trading) Regulations, 2015 and SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to the Securities Market) Regulations, 2003 by the trust, the company and its employees, as applicable.

SHAREHOLDERS APPROVAL

- Scheme shall not be offered to employees of a company unless the shareholders of the company approve it by passing a special resolution in the general meeting.
- The explanatory statement to the notice and the resolution proposed to be passed by shareholders for the schemes shall include the information as specified by SEBI in this regard.
- Approval of shareholders by way of separate resolution in the general meeting shall be obtained by the company in case of:
 - (a) Secondary acquisition for implementation of the schemes.
Such approval shall mention the percentage of secondary acquisition (subject to limits specified under these regulations) that could be undertaken;
 - (b) Secondary acquisition by the trust in case the share capital expands due to capital expansion undertaken by the company including preferential allotment of shares or qualified institutions placement, to maintain the five per cent cap as prescribed in these regulations of such increased capital of the company;
 - (c) Grant of option, SAR, shares or other benefits, as the case may be, to employees of subsidiary or holding company;
 - (d) Grant of option, SAR, shares or benefits, as the case may be, to identified employees, during any one year, equal to or exceeding one per cent of the issued capital (excluding outstanding warrants and conversions) of the company at the time of grant of option, SAR, shares or incentive, as the case may be.

VARIATION OF TERMS OF THE SCHEMES

- The company shall not vary the terms of the schemes in any manner, which may be detrimental to the interests of the employees.
However, the company shall be entitled to vary the terms of the schemes to meet any regulatory requirements.
- The company may by special resolution in general meeting vary the terms of the schemes offered pursuant to an earlier resolution of the general body but not yet exercised by the employee provided such variation is not prejudicial to the interests of the employees.
- The provisions of shareholders' approval shall apply to such variation of terms as they apply to the original grant of option, SAR, shares or other benefits, as the case may be.
- The notice for passing special resolution for variation of terms of the schemes shall disclose full details of the variation, the rationale therefore, and the details of the employees who are beneficiaries of such variation.
- A company may reprise the options, SAR or shares, as the case may be which are not exercised, whether or not they have been vested if the schemes were rendered unattractive due to fall in the price of the shares in the stock market.

However, the company ensures that such repricing shall not be detrimental to the interest of the employees and approval of the shareholders in general meeting has been obtained for such repricing.

WINDING UP OF THE SCHEMES

In case of winding up of the schemes being implemented by a company through trust, the excess monies or shares remaining with the trust after meeting all the obligations, if any, shall be utilised for repayment of loan or by way of distribution to employees as recommended by the compensation committee.

NON-TRANSFERABILITY

- Option, SAR or any other benefit granted to an employee under the regulations shall not be transferable to any person.
- No person other than the employee to whom the option, SAR or other benefit is granted shall be entitled to the benefit arising out of such option, SAR, benefit etc.,

However, in case of ESOS or SAR, under cashless exercise, the company may itself fund or permit the empanelled stock brokers to fund the payment of exercise price which shall be adjusted against the sale proceeds of some or all the shares, subject to the provisions of the applicable law or regulations.

- The option, SAR, or any other benefit granted to the employee shall not be pledged, hypothecated, mortgaged or otherwise alienated in any other manner.
- In the event of death of the employee while in employment, all the options, SAR or any other benefit granted to him under a scheme till such date shall vest in the legal heirs or nominees of the deceased employee.
- In case the employee suffers a permanent incapacity while in employment, all the options, SAR or any other benefit granted to him under a scheme as on the date of permanent incapacitation, shall vest in him on that day.
- In the event of resignation or termination of the employee, all the options, SAR, or any other benefit which are granted and yet not vested as on that day shall expire.

However, an employee shall, subject to the terms and conditions formulated by the compensation committee, be entitled to retain all the vested options, SAR, or any other benefit covered by these regulations.

- In the event that an employee who has been granted benefits under a scheme is transferred or deputed to an associate company prior to vesting or exercise, the vesting and exercise as per the terms of grant shall continue in case of such transferred or deputed employee even after the transfer or deputation.

LISTING

In case new issue of shares is made under any scheme, shares so issued shall be listed immediately in any recognised stock exchange.

In case of the existing shares are listed, subject to the following conditions :-

Scheme is in compliance with these regulations	A statement specified by SEBI in this regard, is filed and the company has obtained an in-principle approval from the stock exchanges	As and when an exercise is made, the company notifies the concerned stock exchange as per the statement as specified by SEBI in this regard
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SCHEMES IMPLEMENTED BY UNLISTED COMPANIES

The shares arising after the initial public offering (“IPO”) of an unlisted company, out of options or SAR granted under any scheme prior to its IPO to the employees shall be listed immediately upon exercise in all the recognised stock exchanges where the shares of the company are listed subject to compliance with SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009.

COMPLIANCES AND CONDITIONS

The company shall not make any fresh grant which involves allotment or transfer of shares to its employees under any schemes formulated prior to its IPO and prior to the listing of its equity shares ('pre-IPO scheme') unless:

- Such pre-IPO scheme is in conformity with these regulations; and
- Such pre-IPO scheme is ratified by its shareholders subsequent to the IPO.

No change shall be made in the terms of options or shares or SAR issued under such pre-IPO schemes, whether by repricing, change in vesting period or maturity or otherwise unless prior approval of the shareholders is taken for such a change, except for any adjustments for corporate actions made in accordance with these regulations.

For listing of shares issued pursuant to ESOS, ESPS or SAR, the company shall obtain the in-principle approval of the stock exchanges where it proposes to list the said shares.

However, the ratification under clause (ii) may be done any time prior to grant of new options or shares or SAR under such pre-IPO scheme.

CERTIFICATE FROM AUDITORS

In case of company which has passed a resolution for the schemes under these regulations, the board of directors shall at each annual general meeting place before the shareholders a certificate from the auditors of the company that the scheme(s) has been implemented in accordance with these regulations and in accordance with the resolution of the company in the general meeting.

DISCLOSURES

In addition to the information that a company is required to disclose, in relation to employee benefits under the Companies Act, 2013, the board of directors of such a company shall also disclose the details of the scheme(s) being implemented, as specified by SEBI in this regard.

ACCOUNTING POLICIES

Any company implementing any of the share based schemes shall follow the requirements of the 'Guidance Note on Accounting for employee share-based Payments' (Guidance Note) or Accounting Standards as may be prescribed by the Institute of Chartered Accountants of India (ICAI) from time to time, including the disclosure requirements prescribed therein.

Where the existing Guidance Note or Accounting Standard do not prescribe accounting treatment or disclosure requirements for any of the schemes covered under these regulations, then the company shall comply with the relevant Accounting Standard as may be prescribed by the ICAI from time to time.

ADMINISTRATION OF SPECIFIC SCHEMES

EMPLOYEE STOCK OPTION SCHEME (ESOS)

Administration and Implementation

The ESOS shall contain the details of the manner in which the scheme will be implemented and operated. ESOS shall not be offered unless the disclosures, as specified by SEBI in this regard, are made by the company to the prospective option grantees.

Pricing

The company granting option to its employees pursuant to ESOS will have the freedom to determine the exercise price subject to conforming to the accounting policies as specified in these regulation.

Vesting Period

There shall be a minimum vesting period of one year in case of ESOS. However, in case where options are granted by a company under an ESOS in lieu of options held by a person under an ESOS in another company which has merged or amalgamated with that company, the period during which the options granted by the transfer or company were held by him shall be adjusted against the minimum vesting period required under this sub-regulation.

The company may specify the lock-in period for the shares issued pursuant to exercise of option.

Rights of the option holder

The employee shall not have right to receive any dividend or to vote or in any manner enjoy the benefits of a shareholder in respect of option granted to him, till shares are issued upon exercise of option.

Consequence of failure to exercise option

The amount payable by the employee, if any, at the time of grant of option, -

- (a) may be forfeited by the company if the option is not exercised by the employee within the exercise period; or
- (b) may be refunded to the employee if the options are not vested due to non-fulfilment of conditions relating to vesting of option as per the ESOS.

EMPLOYEE STOCK PURCHASE SCHEME (ESPS)

Administration and Implementation

The ESPS scheme shall contain the details of the manner in which the scheme will be implemented and operated.

Pricing and Lock-In

The company may determine the price of shares to be issued under an ESPS, provided they conform to the provisions of accounting policies under these regulation. Shares issued under an ESPS shall be locked-in for a minimum period of one year from the date of allotment.

However, in case where shares are allotted by a company under an ESPS in lieu of shares acquired by the same person under an ESPS in another company which has merged or amalgamated with the first mentioned company, the lock-in period already undergone in respect of shares of the transferor company shall be adjusted against the lock-in period required under this sub-regulation.

If ESPS is part of a public issue and the shares are issued to employees at the same price as in the public issue, the shares issued to employees pursuant to ESPS shall not be subject to lock-in.

STOCK APPRECIATION RIGHTS SCHEME (SARS)***Administration and Implementation***

The SAR scheme shall contain the details of the manner in which the scheme will be implemented and operated. The company shall have the freedom to implement cash settled or equity settled SAR scheme. However, in case of equity settled SAR scheme, if the settlement results in fractional shares, then the consideration for fractional shares should be settled in cash.

SAR shall not be offered unless the disclosures, as specified by SEBI in this regard, are made by the company to the prospective SAR grantees.

Vesting

There shall be a minimum vesting period of one year in case of SAR scheme. However, in a case where SAR is granted by a company under a SAR scheme in lieu of SAR held by the same person under a SAR scheme in another company which has merged or amalgamated with the first mentioned company, the period during which the SAR granted by the transferor company were held by the employee shall be adjusted against the minimum vesting period required under this sub-regulation.

Rights of the SAR Holder

The employee shall not have right to receive dividend or to vote or in any manner enjoy the benefits of a shareholder in respect of SAR granted to him.

GENERAL EMPLOYEE BENEFITS SCHEME (GEBS)***Administration and Implementation***

GEBS shall contain the details of the scheme and the manner in which the scheme shall be implemented and operated. At no point in time, the shares of the company or shares of its listed holding company shall exceed ten per cent of the book value or market value or fair value of the total assets of the scheme, whichever is lower, as appearing in its latest balance sheet for the purposes of GEBS.

RETIREMENT BENEFIT SCHEME (RBS)***Administration and Implementation***

Retirement benefit scheme may be implemented by a company provided it is in compliance with these regulations, and provisions of any other law in force in relation to retirement benefits. The retirement benefit scheme shall contain the details of the benefits under the scheme and the manner in which the scheme shall be implemented and operated.

At no point in time, the shares of the company or shares of its listed holding company shall exceed ten per cent of the book value or market value or fair value of the total assets of the scheme, whichever is lower, as appearing in its latest balance sheet for the purposes of RBS.

DIRECTIONS BY SEBI AND ACTION IN CASE OF DEFAULT

SEBI may issue any direction or order or undertake any measure in the interests of the investors or the securities market, and deal with any contravention of these regulations, in exercise of its powers under SEBI Act, 1992, the Securities Contracts (Regulation) Act, 1956 or the Companies Act, 2013 and any statutory modification or re-enactment thereto.

LESSON ROUND UP

- Public Issue of shares means the selling or marketing of shares for subscription by the public by issue of prospectus.
- Public Issue of shares are regulated by SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009.
- All listed companies whose equity shares are listed on a stock exchange and unlisted companies eligible to make a public issue and desirous of getting its securities listed on a recognised stock exchange pursuant to a public issue, may freely price its equity shares or any securities convertible at a later date into equity shares.
- The promoters should contribute not less than 20% of post-issue capital, in case of a public issue by an unlisted company.
- Underwriting means an agreement with or without conditions to subscribe to the securities of a body corporate when the existing shareholders of such body corporate or the public do not subscribe to the securities offered to them.
- In case of a public issue by an unlisted company, at least 10% or 25% of the post issue capital should be offered to the public and a listed company making public issue should make the net offer of at least 10% or 25% of the issue size to the public.
- A merchant banker holding a valid certificate of registration is required to be appointed to manage the issue.
- Every company making a public issue is required to appoint a compliance officer and intimate the name of the compliance officer to SEBI.
- Book Building means a process undertaken by which a demand for the securities proposed to be issued by a body corporate is build up and a 'Fair Price' and 'Quantum' of securities to be issued is finally determined.
- An issuer company making a public offer of equity shares can avail of the Green Shoe Option (GSO) for stabilizing the post listing price of its shares.
- A SME can issue specified securities in accordance with chapter XB of SEBI (ICDR) Regulations, 2009.
- SEBI has stipulated conditions and manner for providing exit opportunity to dissenting shareholders.
- SEBI has inserted a new chapter XC in SEBI (ICDR) Regulations, 2009 for entities. Getting Listing of their securities exclusively in the Institutional Platform either pursuant to a public issues or otherwise.
- Issue of Employee Stock option is regulated by SEBI (Share Based Employee Benefits) Regulations, 2014

GLOSSARY

Average market capitalisation of public shareholding	It means the sum of daily market capitalization of “public shareholding” for a period of one year up to the end of the quarter preceding the month in which the proposed issue was approved by the Board of Directors/ shareholders, as the case may be, divided by the number of trading days.
General Corporate Purpose	It include such identified purposes for which no specific amount is allocated or any amount so specified towards General Corporate Purpose or any such purpose by whatever name called, in the draft offer document filed with SEBI.
Key Management Personnel	It 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.
Retail individual investor	It means an investor who applies or bids for specified securities for a value of not more than two lakhs rupees.
Retail individual shareholder	It means a shareholder of a listed issuer, who applies or bids for specified securities for a value of not more than two lakhs Rupees.

SELF TEST QUESTIONS

1. What is a prospectus? Discuss broadly the disclosures to be made in prospectus.
2. Explain the various legal provisions to be complied with for further issue of capital.
3. Write a note on the work involved in making an issue of share open to the public.
4. State the Regulations relating to Issue of Bonus Shares.
5. What do you understand by Book Building? Explain briefly SEBI's Regulations for 100% book building.
6. Explain briefly about the ASBA process. Who are the eligible investors? State.
7. What are the criteria for issue specified securities by a SME?
8. Write short notes on –
 - (a) Minimum subscription
 - (b) Anchor Investor
 - (c) Minimum promoters' contribution and lock-in-period
 - (d) Preferential allotment
 - (e) Green Shoe Option
 - (f) Employee Stock Option Scheme
 - (g) Self Certified Syndicate Bank.
9. What are the conditions for making Qualified Institutions placement under SEBI ICDR Regulations?
10. What is Institutional Placement Programme (IPP)? Briefly explain the restrictions on making IPP.
11. What are the conditions for providing exit opportunity to dissenting shareholders.

Lesson 21

Regulatory Framework relating to Securities Market Intermediaries

LESSON OUTLINE

Part A

- Introduction
- SEBI (Merchant Bankers) Regulations, 1992
- SEBI (Registrars to an Issue and Share Transfer Agents) Regulations, 1993
- SEBI (Underwriters) Regulations, 1993
- SEBI (Bankers to an Issue) Regulations, 1994
- SEBI (Debenture Trustees) Regulations, 1993
- Syndicate Members
- SEBI (Stock Broker and Sub-Brokers) Regulations, 1992
- Case study on Fraudulent dealings
- Certification by Practising Company Secretary
- SEBI (Portfolio Managers) Regulations, 1993
- SEBI (Custodian of Securities) Regulations, 1996
- SEBI (Investment Advisors) Regulations, 2013

Part B

- Guidelines on Anti-money Laundering Measures
- SEBI (Intermediaries) Regulations, 2008
- SEBI (Research Analyst) Regulations, 2014
- SEBI (Know Your Client) Registration Agency (KRA) Regulations, 2011
- List of SEBI Registered Intermediaries
- Functions and Obligations of an Intermediary
- In-Person Verification (IPV)
- SEBI (Self Regulatory Organisations) Regulations, 2004
- LESSON ROUND UP
- GLOSSARY
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

Intermediaries are service providers and are an integral part of any financial system. The Market Regulator, i.e., SEBI regulates various intermediaries in the primary and secondary markets through its Regulations for these respective intermediaries. SEBI has defined the role of each of the intermediary, the eligibility criteria for granting registration, their functions and responsibilities and the code of conduct to which they are bound. These Regulations also empower SEBI to inspect the functioning of these intermediaries and to collect fees from them and to impose penalties on erring entities.

This lesson, will enable the students to know about the regulatory framework of the intermediaries operating in the Primary and the Secondary markets, Know your client norms prescribed by SEBI, SEBI (Intermediaries) Regulations and Self Regulatory Organisation etc.

INTRODUCTION

The capital market intermediaries are vital link between investor, issuer and regulator. The objective of these intermediaries is to smoothen the process of investment and to establish a link between the investors and the users of funds. Corporations and Governments do not market their securities directly to the investors. Instead, they hire the services of the market intermediaries to represent them to the investors. Investors, particularly small investors, find it difficult to make direct investment. A small investor desiring to invest may not find a willing and desirable borrower. He may not be able to diversify across borrowers to reduce risk. He may not be equipped to assess and monitor the credit risk of borrowers. Market intermediaries help investors to select investments by providing investment consultancy, market analysis and credit rating of investment instruments. In order to operate in secondary market, the investors have to transact through share brokers. Registrars and Share Transfer Agents, Custodians and Depositories are capital market intermediaries that provide important infrastructure services for both primary and secondary markets.

According to SEBI (Intermediaries) Regulations, 2008, “intermediary” means a person mentioned in clauses (b) and (ba) of sub-section (2) of section 11 and sub-section (1) and (1A) of section 12 of the Act and includes an asset management company in relation to the SEBI (Mutual Funds) Regulations, 1996, a clearing member of a clearing corporation or clearing house and a trading member of a derivative segment or currency derivatives segment of a stock exchange **but does not include foreign institutional investor, foreign venture capital investor, mutual fund, collective investment scheme and venture capital fund.**

The market Regulator, SEBI regulates various intermediaries in the primary and secondary markets through its Regulations for these intermediaries. SEBI has defined the role of each of the intermediary, the eligibility criteria for granting registration, their functions and responsibilities and the code of conduct to which they are bound. These Regulations also empower SEBI to inspect the functioning of these intermediaries and to collect fees from them and to impose penalties on erring entities. As per Section 11 of SEBI Act, it is the duty of SEBI to register and regulate the working of stock brokers, sub-brokers, share transfer agents, bankers to an issue, trustees of trust deeds, registrars to an issue, merchant bankers, underwriters, portfolio managers, investment advisers and such other intermediaries who may be associated with securities market in any manner.

SEBI has issued regulations in respect of each intermediary to ensure proper services to be rendered by them to the investors and the capital market which is discussed below.

ROLE OF CAPITAL MARKET INTERMEDIARIES

The role of intermediaries makes the market vibrant, and to function smoothly and continuously. Intermediaries possess professional expertise and play a promotional role in organising a perfect match between the supply and demand for capital in the market. All those, institutions or individuals, who help to bring the savers and seekers of capital and enable a regular flow of funds from supply to demand points are intermediaries. All intermediaries are service providers and are an integral part of the Securities Market.

These market intermediaries provide different types of financial services to the investors. They are constantly operating in the financial market. It is in their (market intermediaries) own interest to behave rationally, maintain integrity and to protect and maintain reputation, otherwise the investors would not be trusting them next time. In principle, these intermediaries bring efficiency to corporate fund raising by developing expertise in pricing new issues and marketing them to the investors.

Presently this lesson briefly covers in a nutshell the core functions of each one of the intermediaries operating in the Primary and the Secondary markets.

The following market intermediaries are involved in the Securities Market:

- Merchant Bankers

- Registrars and Share Transfer Agents
- Underwriters
- Bankers to an issue
- Debenture Trustees
- Syndicate members
- Stock-brokers and sub-brokers
- Portfolio managers
- Custodians of Securities
- Investment Advisers
- Research Analysts
- Credit Rating Agencies
- Depository Participant

MERCHANT BANKERS

'Merchant Banker' means any person engaged in the business of issue management by making arrangements regarding selling buying or subscribing to securities or acting as manager/consultant/advisor or rendering corporate advisory services in relation to such issue management.

Among the important financial intermediaries are the merchant bankers. They are the key intermediary between the company and issue of capital. It is quite common to come across reference to Merchant Banking and financial services as though they are distinct categories. The services provided by Merchant Bankers depend on their inclination and resources - technical and financial. Merchant bankers (Category I) are mandated by SEBI to manage public issues. These activities have major implications for the integrity of the market. They affect investors' interest and, therefore, transparency has to be ensured. Merchant Bankers are rendering diverse services and functions. These include organising and extending finance for investment in projects, assistance in financial management, raising Euro dollar loans and issue of foreign currency bonds. Different merchant bankers specialised in different services.

SEBI has advised that merchant bankers shall undertake only those activities which relate to securities market. These activities are:

- (a) Managing of public issue of securities;
- (b) Underwriting connected with the aforesaid public issue management business;
- (c) Managing/Advising on international offerings of debt/equity i.e. GDR, ADR, bonds and other instruments;
- (d) Private placement of securities;
- (e) Primary or satellite dealership of government securities;
- (f) Corporate advisory services related to securities market including takeovers, acquisition and disinvestment;
- (g) Stock broking;
- (h) Advisory services for projects;
- (i) Syndication of rupee term loans;
- (j) International financial advisory services.

The activities of the Merchant Bankers in the Indian capital market are regulated by SEBI (Merchant Bankers) Regulations, 1992.

SEBI (MERCHANT BANKERS) REGULATIONS, 1992

The activities of the merchant bankers in the Indian capital market are regulated by SEBI (Merchant Bankers) Regulations, 1992.

Regulation 3 of SEBI (Merchant Bankers) Regulations, 1992 lays down that an application by a person desiring to become merchant banker shall be made to SEBI in the prescribed form (Form A) seeking grant of a certificate of registration alongwith a non-refundable application fee as specified in Schedule II of these Regulations.

The aforesaid application shall be made for any one of the following categories of the merchant banker namely:–

- (a) Category I, that is –
 - (i) to carry on any activity of the issue management, which will, inter alia, consist of preparation of prospectus and other information relating to the issue, determining financial structure, tie up of financiers and final allotment and refund of the subscriptions; and
 - (ii) to act as adviser, consultant, manager, underwriter, portfolio manager;
- (b) Category II, that is to act as adviser, consultant, co-manager, underwriter, portfolio manager;
- (c) Category III, that is to act as underwriter, adviser, consultant to an issue;
- (d) Category IV, that is to act only as adviser or consultant to an issue.

Regulation 4 and 5 deal with the methodology for application and furnishing of information, clarification and personal representation by the applicant. Incomplete or non-conforming applications shall be rejected after giving an opportunity to remove the deficiencies within a time specified by SEBI and the applicant shall furnish further information or clarification to SEBI regarding matters relevant to the activity of a merchant banker of the purpose of disposal of the application.

Regulation 6 lists out the following considerations for being taken into account by SEBI to grant the certificate of registration.

- (a) the applicant shall be a body corporate other than a non-banking financial company as defined under clause(f) of section 45-I of the RBI Act, 1934;

However, the Merchant Banker who has been granted registration by the RBI to act as a primary or satellite dealer may carry on such activity subject to the condition that it shall not accept or hold public deposit;
- (aa) the applicant has the necessary infrastructure like adequate office space equipments, and manpower to effectively discharge his activities.
- (b) the applicant has in his employment a minimum of two persons who have the experience to conduct the business of the merchant banker;
- (c) a person directly or indirectly connected with the applicant has not been granted registration by SEBI;

(Here the expression “directly or indirectly connected” means any person being an associate, subsidiary or interconnected or group company of the applicant in case of the applicant being a body corporate)
- (d) the applicant fulfills the capital adequacy requirement;
- (e) the applicant, his partner, director or principal officer is not involved in any litigation connected with the securities market which has an adverse bearing on the business of the applicant;
- (f) the applicant, his director, partner or principal officer has not at any time been convicted for any offence involving moral turpitude or has been found guilty of any offence;

- (g) the applicant has the professional qualification from an institution recognised by the Government in finance, law or business management;
- (h) the applicant is a fit and proper person;
- (i) grant of certificate to the applicant is in the interest of investors.

Regulation 7 prescribes that the capital adequacy requirement shall be a networth of not less than five crore rupees.

(‘Networth’ means the sum of paid-up capital and free reserves of the applicant at the time of making application.)

Regulation 8 deals with grant of certificate of registration, where SEBI is satisfied that applicant is eligible, shall grant certificate of registration in Form B and intimate the same information to the applicant. The certificate of registration granted shall be valid unless it is suspended or cancelled by SEBI.

Regulation 9A and 10 deals with conditions of registration for initial registration (granted under regulation 8) and procedure where registration is not granted.

Regulation 8, 9A and 10 deal with procedure for registration, renewal of certificate conditions of registration and procedure where registration is not granted.

However, SEBI may, in the interest of investors in the securities market, permit the merchant banker to carry on activities undertaken prior to the receipt of the intimation of refusal subject to such condition as the SEBI may specify.

Regulation 12 provides for payment of fees and consequences of failure to pay annual fees. It provides that SEBI may suspend the registration certificate if merchant banker fails to pay fees.

GENERAL OBLIGATIONS AND RESPONSIBILITIES OF MERCHANT BANKER

Chapter III of the Regulations containing Regulations 13 to 28 deal with general obligations and responsibilities of Merchant Bankers.

Regulation 13 stipulates that every merchant banker shall abide by the code of conduct which has been specified in Schedule III. The code of conduct as provided in the schedule is as under:

Code of Conduct for Merchant Bankers

1. A merchant banker shall make all efforts to protect the interests of investors.
2. A merchant banker shall maintain high standards of integrity, dignity and fairness in the conduct of its business.
3. A merchant banker shall fulfil its obligations in a prompt, ethical, and professional manner.
4. A merchant banker shall at all times exercise due diligence, ensure proper care and exercise independent professional judgement.
5. A merchant banker shall endeavour to ensure that –
 - (a) inquiries from investors are adequately dealt with;
 - (b) grievances of investors are redressed in a timely and appropriate manner;
 - (c) where a complaint is not remedied promptly, the investor is advised of any further steps which may be available to the investor under the regulatory system.
6. A merchant banker shall ensure that adequate disclosures are made to the investors in a timely manner in accordance with the applicable regulations and guidelines so as to enable them to make a balanced and informed decision.

7. A merchant banker shall endeavour to ensure that the investors are provided with true and adequate information without making any misleading or exaggerated claims or any misrepresentation and are made aware of the attendant risks before taking any investment decision.
8. A merchant banker shall endeavour to ensure that copies of the prospectus, offer document, letter of offer or any other related literature is made available to the investors at the time of issue or the offer.
9. A merchant banker shall not discriminate amongst its clients, save and except on ethical and commercial considerations.
10. A merchant banker shall not make any statement, either oral or written, which would misrepresent the services that the merchant banker is capable of performing for any client or has rendered to any client.
11. A merchant banker shall avoid conflict of interest and make adequate disclosure of its interest.
12. A merchant banker shall put in place a mechanism to resolve any conflict of interest situation that may arise in the conduct of its business or where any conflict of interest arises, shall take reasonable steps to resolve the same in an equitable manner.
13. A merchant banker shall make appropriate disclosure to the client of its possible source or potential areas of conflict of duties and interest while acting as merchant banker which would impair its ability to render fair, objective and unbiased services.
14. A merchant banker shall always endeavour to render the best possible advice to the clients having regard to their needs.
15. A merchant banker shall not divulge to anybody either orally or in writing, directly or indirectly, any confidential information about its clients which has come to its knowledge, without taking prior permission of its clients, except where such disclosures are required to be made in compliance with any law for the time being in force.
16. A merchant banker shall ensure that any change in registration status/any penal action taken by the SEBI or any material change in the merchant banker's financial status, which may adversely affect the interests of clients/ investors is promptly informed to the clients and any business remaining outstanding is transferred to another registered intermediary in accordance with any instructions of the affected clients.
17. A merchant banker shall not indulge in any unfair competition, such as weaning away the clients on assurance of higher premium or advantageous offer price or which is likely to harm the interests of other merchant bankers or investors or is likely to place such other merchant bankers in a disadvantageous position while competing for or executing any assignment.
18. A merchant banker shall maintain arms length relationship between its merchant banking activity and any other activity.
19. A merchant banker shall have internal control procedures and financial and operational capabilities which can be reasonably expected to protect its operations, its clients, investors and other registered entities from financial loss arising from theft, fraud, and other dishonest acts, professional misconduct or omissions.
20. A merchant banker shall not make untrue statement or suppress any material fact in any documents, reports or information furnished to SEBI.
21. A merchant banker shall maintain an appropriate level of knowledge and competence and abide by the provisions of the Act, regulations made thereunder, circulars and guidelines, which may be applicable and relevant to the activities carried on by it. The merchant banker shall also comply with the award of the Ombudsman passed under the SEBI (Ombudsman) Regulations, 2003.
22. A merchant banker shall ensure that SEBI is promptly informed about any action, legal proceedings,

etc., initiated against it in respect of material breach or non-compliance by it, of any law, rules, regulations, directions of SEBI or of any other regulatory body.

23. (a) A merchant banker or any of its employees shall not render, directly or indirectly, any investment advice about any security in any publicly accessible media, whether real-time or non-real-time, unless a disclosure of his interest including a long or short position, in the said security has been made, while rendering such advice.

(b) In the event of an employee of the merchant banker rendering such advice, the merchant banker shall ensure that such employee shall also disclose the interests, if any, of himself, his dependent family members and the employer merchant banker, including their long or short position in the said security, while rendering such advice.
24. A merchant banker shall demarcate the responsibilities of the various intermediaries appointed by it clearly so as to avoid any conflict or confusion in their job description.
25. A merchant banker shall provide adequate freedom and powers to its compliance officer for the effective discharge of the compliance officer's duties.
26. A merchant banker shall develop its own internal code of conduct for governing its internal operations and laying down its standards of appropriate conduct for its employees and officers in carrying out their duties. Such a code may extend to the maintenance of professional excellence and standards, integrity, confidentiality, objectivity, avoidance or resolution of conflict of interests, disclosure of shareholdings and interests, etc.
27. A merchant banker shall ensure that good corporate policies and corporate governance are in place.
28. A merchant banker shall ensure that any person it employs or appoints to conduct business is fit and proper and otherwise qualified to act in the capacity so employed or appointed (including having relevant professional training or experience).
29. A merchant banker shall ensure that it has adequate resources to supervise diligently and does supervise diligently persons employed or appointed by it in the conduct of its business, in respect of dealings in securities market.
30. A merchant banker shall be responsible for the Acts or omissions of its employees and agents in respect of the conduct of its business.
31. A merchant banker shall ensure that the senior management, particularly decision makers have access to all relevant information about the business on a timely basis.
32. A merchant banker shall not be a party to or instrument for—
 - (a) creation of false market;
 - (b) price rigging or manipulation; or
 - (c) passing of unpublished price sensitive information in respect of securities which are listed and proposed to be listed in any stock exchange to any person or intermediary in the securities market.

Regulation 13A provides that no merchant banker other than a bank or a public financial institution who has been granted a certificate of registration shall carry on any business other than that of the securities market. However, a merchant banker who has been granted certificate of registration under these regulations may ensure market making in accordance with Chapter XB of SEBI (ICDR) Regulations, 2009.

Regulations 14 to 17 deal with maintenance of books of accounts, records, submission of half-yearly results, rectifying deficiencies pointed out in the auditors report etc.

RESPONSIBILITIES OF LEAD MANAGERS

Regulation 20 provides that no lead manager shall agree to manage or be associated with any issue unless his responsibilities relating to the issue mainly those of disclosures, allotment and refund are clearly defined, allocated and determined and a statement specifying such responsibilities is furnished to SEBI at least 1 month before the opening of the issue for subscription but where there are more than 1 lead merchant banker to the issue the responsibility of each such lead merchant banker shall clearly be demarcated and the statement specifying such responsibilities shall be furnished to SEBI at least 1 month before the opening of the issue for subscription.

MERCHANT BANKER NOT TO ACT AS SUCH FOR AN ASSOCIATE

Regulation 21 stipulates that a lead merchant banker shall not associate himself with any issue if a merchant banker not holding a certificate from SEBI is associated with the issue.

Regulation 21A provides that a merchant banker shall not lead manage any issue or be associated with any activity undertaken under any regulations made by SEBI, if he is a promoter or a director or an associate of the issuer of securities or of any person making an offer to sell or purchase securities. However, a merchant banker who is an associate of such issuer or person may be appointed, if he is involved only in the marketing of the issue or offer.

Here, a merchant banker shall be deemed to be an “associate of the issuer or person” if:

- (i) either of them controls, directly or indirectly through its subsidiary or holding company, not less than 15% of the voting rights in the other; or
- (ii) either of them, directly or indirectly, by itself or in combination with other persons, exercises control over the other; or
- (iii) there is a common director, excluding nominee director, amongst the issuer, its subsidiary or holding company and the merchant banker.

MINIMUM UNDERWRITING OBLIGATION

Regulation 22 lays down that in respect of every issue to be managed, the lead merchant banker holding a certificate under Category I shall accept a minimum underwriting obligation of 5% of the total underwriting commitment or ₹ 25 lakhs whichever is less but if the lead merchant banker is unable to accept the minimum underwriting obligation, that lead merchant banker shall make arrangement for having the issue underwritten to that extent by a merchant banker associated with the issue and shall keep SEBI informed of such arrangement. In case of issue made in accordance with Chapter XA of SEBI (ICDR) Regulations, 2009, the merchant banker shall itself or jointly with other merchant bankers associated with the issues, underwrite atleast 15% of the issue size.

PROHIBITION TO ACQUIRE SHARES

Regulations 26 and 27 deal with this matter.

Regulation 26 lays down that no merchant banker or any of its directors, partners or manager or principal officer shall either on their own account or through their associates or relatives, enter into any transaction in securities of bodies corporate on the basis of unpublished price sensitive information obtained by them during the course of any professional assignment either from the clients or otherwise.

Regulation 27 requires every merchant banker to submit to SEBI complete particulars of any transaction for acquisition of securities of any body corporate whose issue is being managed by that merchant banker, within 15 days from the date of entering into such transaction. In case of any transaction for acquisition of securities made in pursuance of underwriting or market making obligation in accordance with Chapter XA of SEBI (ICDR) Regulations, 2009, the complete particulars of the transaction shall be submitted to SEBI on quarterly basis.

DISCLOSURE TO SEBI

Regulation 28 provides that a merchant banker is required to disclose to SEBI, as and when required, the following information, namely :

- (i) his responsibilities with regard to the management of the issue;
- (ii) any change in the information or particulars previously furnished, which have a bearing on the certificate granted to it;
- (iii) the names of the body corporate whose issues he has managed or has been associated with;
- (iv) the particulars relating to the breach of the capital adequacy requirement;
- (v) relating to his activities as a manager, underwriter, consultant or adviser to an issue, as the case may be.

The merchant banker shall submit a periodic report in such manner as may be specified by SEBI from time to time.

APPOINTMENT OF COMPLIANCE OFFICER

Regulation 28A requires every merchant banker to appoint a compliance officer who shall be responsible for monitoring the compliance of the Act, rules and regulations, notifications, guidelines, instructions etc. issued by SEBI or Central Government and for redressal of investor grievances. Compliance officer is required to immediately and independently report to SEBI, any non-compliance observed by him and ensure that observations made or deficiencies pointed out by SEBI on/in the draft prospectus or letter of offer as the case may be, do not occur.

PROCEDURE FOR INSPECTION

Chapter IV containing Regulations 29 to 34 lays down the procedure for inspection of the merchant bankers offices and records by SEBI.

Regulation 29 empowers SEBI to appoint one or more persons as inspecting authority to undertake inspection of books of accounts, records etc. of the merchant banker, to ensure that such books and records are maintained in the prescribed manner, the provisions of SEBI Act and the rules and regulations thereunder are complied with to investigate into complaints from investors, other merchant bankers or other persons on any matter having a bearing on the activities of the merchant banker and to investigate suo motu in the interest of the securities business or investors interest into the working of the merchant banker.

Regulation 30 and 31 authorise SEBI to undertake such inspection with or without notice and the obligations of the merchant bankers in relation to such inspection.

Regulation 32 provides for the submission of an inspection report to SEBI by the inspecting authority on completion of inspection. Regulation 33 requires that SEBI or chairman shall after consideration of inspection or investigation report take such action as SEBI or chairman may deem fit and appropriate including action under Chapter V of the SEBI (Intermediaries) Regulations, 2008.

Regulation 34 permits SEBI to appoint a qualified auditor to investigate into the books of accounts or the affairs of the merchant banker and such auditor shall have the same powers of the inspecting authority referred to above.

PROCEDURE FOR ACTION AGAINST MERCHANT BANKER IN CASE OF DEFAULT

Chapter V containing Regulation 35 deals with the procedure for taking action against the merchant banker in case of default.

Regulation 35 provides that a merchant banker who contravenes any of the provisions of the Act, rules or regulations, framed thereunder shall be liable for one or more actions specified therein including the action under Chapter V of SEBI (Intermediaries) Regulations, 2008.

REGISTRARS AND SHARE TRANSFER AGENTS

‘Registrar to an Issue’ means the person appointed by a body corporate or any person or group of persons to carry on the following activities on its or his or their behalf i.e.:

- (i) collecting application for investor in respect of an issue;
- (ii) keeping a proper record of applications and monies received from investors or paid to the seller of the securities;
- (iii) (a) assisting body corporate or person or group of persons in determining the basis of allotment of the securities in consultation with the stock exchange;
- (b) finalising the list of person entitled to allotment of securities;
- (c) processing and despatchment of allotment letters, refund orders or certificates and other related documents in respect of the issue;

‘Share Transfer Agent’ means:

- (i) any person who on behalf of any body corporate, maintains the records of holders of securities issued by such body corporate and deals with all matters connected with the transfer and redemption of its securities;
- (ii) the department or division, by whatever name called, of a body corporate performing the activities as share transfer agents if at any time the total number of holders of its securities issued exceed one lakh.

The Registrars to an Issue and Share Transfer Agents constitute an important category of intermediaries in the primary market. They render very useful services in mobilising new capital and facilitating proper records of the details of the investors, so that the basis for allotment could be decided and allotment ensured as per SEBI Regulations.

They also render service to the existing companies in servicing the share capital contributed by the investors. The system of share transfers gives liquidity to the investment and helps the investors to easily acquire or dispose off shares in the secondary market. The share transfer agents who have the necessary expertise, trained staff, reliable infrastructure and SEBI licence render service to the corporates by undertaking and executing the transfer and transmission work relating to the company’s shares and securities. Thus, they have a role to play both in the primary and the secondary markets.

Pre-issue Activities

- Sending instructions to Banks for reporting of collection figures and collection of applications.
- Providing Practical inputs to the Lead Manager and Printers regarding the design of the Bid cum-Application form.
- Facilitate and establish information flow system between clients , Banks and Managers to the issue.
- Liaison with Regulatory Authorities such as SEBI & Stock Exchanges.

Activities during the Issue

- Collection and Reporting of daily Collection figures.
- Collection of Data and Forms from Banks.

- Liaising with clients and Intermediaries to the Issue.

Post Issue Activities

- Data capturing & validation.
- Reconciliation.
- Provide Allotment Alternatives in consultation with Client / Merchant Banker and Stock Exchanges.
- Facilitating Listing.
- Filing of Return of Allotment.
- Uploading of data to the Depositories for crediting of securities electronically.
- Dispatch of Refund orders / Share Certificates / Credit Advise.
- Periodic Report submission to Regulatory Authorities.
- Reconciliation of Refund payments.
- Attending to post issue Investor queries.
- Web-based investor enquiry system for allotment / refund details.

Share Transfer Agent Services

- Processing of transfer of securities in physical form.
- Processing Transmission / Transposition / Consolidation of holdings.
- Processing of demat requests and converting physical holding into electronic holding (dematerialization).
- Processing of remat requests and converting electronic holding into physical holding (rematerialization)
- Recording of specimen signatures in electronic media.
- Recording of Change of address, Bank Mandates and ECS requests received from investors in physical mode.
- Accurate scanning and capturing of data.
- Issue of Duplicate/split/Consolidated Share Certificates .
- Registration of Nomination.
- Registration of Legal documents such as Power of Attorney etc.
- Dividend payout management services.
- Maintenance of Records of Inward/Outward.
- Maintain and upkeep of statutory records such as Transfer Deeds , Demat / Remat Request Form, Register of Members , Allotment Registers , undelivered returned security documents and other Registers and Returns.
- Processing of Call payments and Endorsements.
- Investor Services including providing investor related information, across counters through written communication and through telephone and via e-mail.
- Integrating electronic beneficiary positions with the physical shareholding.
- Redress Investor Complaints which appears in SEBI Complaints Redress System (SCORES).

- Assisting Client Companies in the redressing investor grievances which appears in their ID.

SEBI (REGISTRARS TO AN ISSUE AND SHARE TRANSFER AGENTS) REGULATIONS, 1993

SEBI (Registrars to an Issue and Share Transfer Agents) Regulations, 1993 were notified by SEBI on 31st May, 1993 in exercise of the powers conferred by Section 30 of SEBI Act, 1992, with the approval of Central Government.

Chapter I of the Regulations contains preliminary items and Chapter II consisting of Regulations 3 to 12 dealing with procedure for applying for registration as Registrar to an Issue (RTI) and Share Transfer Agents (STA), either as Category-I to carry on both the activities of RTA and STA or Category-II to carry on the activity either as Registrar to an Issue or as a Share Transfer Agent. The application should be complete and conform to the requirements otherwise it will be rejected. But an opportunity will be given to remove the objections as may be indicated by SEBI. In case of failure the application may be rejected.

CRITERIA FOR REGISTRATION

Regulation 6 lays down that SEBI shall take into account the following matters while considering the applications for registration. It shall assess whether the applicant:

- has the necessary infrastructure like adequate office space, equipments and manpower to effectively discharge his activities;
- has any past experience in the activities;
- any person directly or indirectly connected with him has been granted registration by SEBI under the Act;
- fulfills the capital adequacy requirement;
- has been subjected to any disciplinary proceedings under the Act;
- any of its director, partner or principal officer is or has at any time been convicted for any offence involving moral turpitude or has been found guilty of any economic offence;
- is a fit and proper person.

Regulation 7 stipulates the capital adequacy requirement (networth) for category I as ₹ 50,00,000 and category II as ₹ 25,00,000.

Regulations 8 to 10 lay down the procedure for registration, renewal of certificate, conditions of registration, period of validity of certificate and the procedure where registration is not granted. It is made clear that the applicant will be given due opportunity of being heard before rejection of his application.

Regulation 12 prescribes payment of fees and indicates the consequences of failure to pay fees. In the latter case SEBI may suspend the certificate with the consequence that the RTA shall cease to carry on his activity from the date of suspension of the certificate.

GENERAL OBLIGATIONS AND RESPONSIBILITIES

Chapter III consisting of Regulations 13 to 15 lays down the general obligations and responsibilities of RTAs.

Specified in Schedule III of these regulations.

Regulation 13A prohibits an RTA from acting as such Registrar in case he or it is an associate of the body corporate issuing the securities. For the purposes of this regulation, Registrar to an Issue or the body corporate, as the case may be, shall be deemed to be an associate of other where –

- (i) he or it controls directly or indirectly not less than 10% of the voting power of the body corporate or of Registrar to an issue, as the case may be or
- (ii) he or any of his relative is a director or promoter of the body corporate or of the Registrar to an Issue, as the case may be. The term 'relative' shall have the same meaning as assigned to it under Section 2(77) of the Companies Act, 2013.

The RTA has to maintain proper books and records as prescribed in Regulation 14 and preserve the account books and other records for a minimum period of 3 years. Regulation 15A provides that every Registrar to an Issue and Share Transfer Agent shall appoint a compliance officer who shall be responsible for monitoring the compliance of the Act, rules and regulations, notifications, guidelines, instructions etc. issued by SEBI or Central Government and for redressal of investor grievances. Compliance officer shall immediately and independently report to SEBI any non-compliance observed by him.

PROCEDURE FOR INSPECTION

Chapter IV containing Regulation 16 to 21 deals with procedure for inspection by SEBI appointed inspecting authority to ensure that the books of accounts and documents are maintained as prescribed and that the provisions of SEBI Act and the rules and regulations there under are complied with. Investigation may be undertaken on the basis of complaints received from the investors, other registrars or any other intermediaries in respect of RTA as prescribed in regulation 16.

Regulation 17 authorise SEBI to undertake such inspection with or without notice and Regulation 18 indicates the obligations of the RTA in relation to such inspection/investigation.

Regulations 19 and 20 stipulate that the inspecting authority shall on the conclusion of his inspection submit a report to SEBI. SEBI after considering the inspection or investigation report take such action as SEBI or chairman may deem fit and appropriate including action under Chapter V of SEBI (Intermediaries) Regulations, 2008.

Regulation 21 authorises SEBI to appoint an Auditor to investigate into the books of account or the affairs of the RTA and STA. The Auditor shall have the same powers as SEBI appointed inspecting authority.

LIABILITY FOR ACTION IN CASE OF DEFAULT

Regulation 22 stipulates the provisions for liability for action in case of default. A Registrar to an Issue who –

- (i) fails to comply with any conditions subject to which registration has been granted.
- (ii) contravenes any of the provisions of the Act, rules or regulations.
- (iii) contravenes the provisions of the SCRA and the rules made thereunder, provisions of the Depositories Act, 1996 or rules made thereunder, the rules, regulations or bye laws of the stock exchange, shall be dealt with in the manner provided in Chapter V of the SEBI (Intermediaries) Regulations, 2008.

UNDERWRITERS

Underwriter means a person who engages in the business of underwriting of an issue of securities of a body corporate.

Underwriting is an arrangement whereby certain parties assure the issuing company to take up shares, debentures or other securities to a specified extent in case the public subscription does not amount to the expected levels. For this purpose, an arrangement (agreement) will be entered into between the issuing company and the assuring party such as a financial institution, banks, merchant banker, broker or other person.

Underwriting is compulsory for a public issue. It is necessary for a public company which invites public subscription for its securities to ensure that its issue is fully subscribed. The company cannot depend on its advertisements to bring in the full subscription. In case of any short-fall, it has to be made good by underwriting arrangements made in advance of the opening of the public issue.

It is the underwriter who agrees to take up securities which are not fully subscribed in a public issue. The underwriter makes a commitment to get the issue subscribing either by others or by themselves.

The lead managers are required to satisfy themselves about the network of the underwriters and their outstanding commitments and disclose the same to SEBI. In this connection, each underwriter should furnish an undertaking to the lead manager about their network and outstanding commitments. Both the lead managers and the directors are required to give a statement in the prospectus that in their opinion the underwriters have the necessary resources to discharge their liabilities, if any, in full. Penal action will be taken against underwriters for not taking up the assured amount of security in case of development and to debar them from the underwriting public issues in future.

SEBI (UNDERWRITERS) REGULATIONS, 1993

These regulations were notified by SEBI in exercise of the powers conferred by Section 30 of SEBI Act, 1992 with the approval of Central Government. They came into force from 8th October, 1993.

Chapter I contains preliminary matters including definitions.

Chapter II deals with the procedure for registration of underwriters and it contains Regulations 3 to 12.

Regulation 3 lays down that the applicant seeking the certificate shall apply to SEBI in form A. Regulation 4 and 5 requires the applicant to furnish further information and clarification to SEBI regarding matters relevant to underwriting. If SEBI on receipt of further information is of the opinion that the information so furnished is not sufficient to decide on the application and seeking further information through correspondence may delay the matter, it may require the applicant or its principal officer to appear before SEBI in order to give an opportunity to the applicant to give further clarifications on the application.

Regulation 5 provides that an application not complete in all respects and not conforming to instructions specified in the form would be rejected. The applicant would be given an opportunity to remove within one month, the objections as may be indicated by SEBI. SEBI may however extend the time by another one month in order to enable the applicant to comply with the requirements of SEBI.

Regulation 6 prescribes the following conditions for consideration of the application:

1. the applicant shall have necessary infrastructure like adequate office space, equipments and manpower and past experience in underwriting, employing at least two persons with such experience. No person directly or indirectly connected with the applicant should have been granted registration by SEBI.

SEBI shall take into account whether a previous application for a certificate of any person directly or indirectly connected with the applicant has been rejected by SEBI or any disciplinary action has been taken against such person under the Act or any rules/regulations.

2. the applicant should be a fit and proper person, fulfilling the capital adequacy requirements and no director, partner or principal officer should have been at any time convicted for an offence involving moral turpitude or found guilty of any economic offence.

Regulation 7 prescribes for the following capital adequacy requirement:

1. The network should not be less than ₹ 20 lakhs.
2. The stock broker who acts as a underwriter should have capital adequacy as prescribed by the stock exchange of which he is a member.

Regulations 8 and 9A, deal with grant of certificate of registration and conditions of registration.

Regulation 10 deal with the procedure where registration is not granted. Regulation 12 prescribes fees payable and consequences of failure to pay fees.

OBLIGATIONS AND RESPONSIBILITIES OF UNDERWRITERS

Chapter III consisting of Regulation 13 to 18 deals with these matters. Every underwriter shall abide by the code of conduct at all times.

Regulations 14 and 15 contain provisions regarding the matters on which every underwriter shall enter into an agreement with the body corporate and his general responsibilities.

The contents of the agreement shall include the period of agreement, the allocation of duties and responsibilities between the underwriter and the client, the amount of underwriting obligations, the period by which the underwriter should subscribe, the amount of commission/brokerage payable, and other details of arrangement for fulfilling the underwriting obligations. The general responsibilities of the underwriter are as follows:

1. The underwriter shall not derive any direct or indirect benefit from underwriting the issue other than the commission or brokerage payable under an agreement for underwriting.
2. The total underwriting obligations under all the agreements shall not exceed 20 times the networth.
3. Every underwriter, in the event of being called upon to subscribe for securities of a body corporate pursuant to an agreement shall subscribe to such securities within 45 days of the receipt of such intimation from such body corporate.

Regulation 16 to 18 relate to maintenance of proper books of account and records and their preservation for 5 years and SEBI's power call for and obtain information from the underwriter.

APPOINTMENT OF COMPLIANCE OFFICER

Regulation 17A requires every underwriter to appoint a compliance officer responsible for monitoring the compliance of the Act, rules and regulations, notifications, guidelines, instructions etc. issued by SEBI or the Central Government and for redressal of investors' grievances. The compliance officer is required to report to SEBI immediately and independently any non-compliance observed by him.

INSPECTION AND DISCIPLINARY PROCEEDINGS

Chapter IV containing Regulations 19 to 24 deals with inspection and disciplinary proceeding. SEBI is empowered to appoint inspectors to ensure that books of accounts, records etc. are maintained properly and the Act along with the rules and regulations are duly complied with. SEBI is also empowered to investigate into complaints received from investors, other underwriters etc. as well as under their own power to investigate *suo motu* in the interest of securities business and the investors.

Regulations 20 and 21 lay down the procedure for inspection and obligations of underwriter during such inspections.

Regulations 22 relate to submission of inspection report to SEBI.

Regulation 23 provides that SEBI or the chairman after the consideration of inspection or investigation report may take action under Chapter V of SEBI (Intermediaries) Regulations, 2008.

Regulation 24 authorised the SEBI to appoint a qualified auditor to investigate into the affairs and the accounts of the underwriter with the same powers as applicable in the case of SEBI appointed inspecting authority.

PROCEDURE FOR ACTION IN CASE OF DEFAULT

Chapter V containing Regulation 25 lays down the procedure for action in case of default. An underwriter who contravenes any of the provisions of the Act, rules or regulations, shall be dealt with in the manner provided under Chapter V of SEBI (Intermediaries) Regulations, 2008.

BANKERS TO AN ISSUE

Banker to an Issue means a scheduled bank carrying on all or any of the following activities:

- (i) Acceptance of application and application monies;
- (ii) Acceptance of allotment or call monies;
- (iii) Refund of application monies;
- (iv) Payment of dividend or interest warrants.

Bankers to the issue, as the name suggests, carries out all the activities of ensuring that the funds are collected and transferred to the Escrow accounts. The Banks render crucial service in mobilisation of capital for companies. While one or more banks may function as Bankers to the Issue as well as collection banks, others may do the limited work of collecting the applications for securities along with the remittance in their numerous branches in different centres. The banks are expected to furnish prompt information and records to the company and to the lead manager for monitoring and progressing the issue work. For this purpose, the company has to enter into an agreement with different banks specifying the conditions, terms and remuneration for services to be rendered by each such bank.

SEBI (BANKERS TO AN ISSUE) REGULATIONS, 1994

SEBI notified these regulations effected from 14th July, 1994 in exercise of the powers conferred by Section 30 of SEBI Act, 1994 after approval by the Central Government.

Chapter I deals with preliminary matters and definitions.

Chapter II containing Regulations 3 to 11 deals with procedure of registration for Bankers to an Issue with SEBI.

Regulations 3 to 5 prescribe that the application by a scheduled bank for grant of certificate of registration as a banker to an issue should be made to SEBI in Form A conforming to the instructions therein failing which, it shall be rejected after giving due opportunity to remove such defects within specified time. SEBI may call for and obtain further information or clarification from the applicant.

CONSIDERATION OF APPLICATION

Regulation 6 prescribes the matters that are considered by SEBI in relation to the application:

- (a) the applicant has the necessary infrastructure, communication and data processing facilities and manpower to effectively discharge his activities;
- (b) the applicant or any of its directors is not involved in any litigation connected with the securities market and which has an adverse bearing on the business of the applicant or has not been convicted of any economic offence;
- (c) the applicant is a scheduled bank;
- (d) the applicant is a fit and proper person;
- (e) grant of certificate to the applicant is in the interest of investors.

PROCEDURE FOR REGISTRATION

Regulations 7 and 8A deals with the grant of certificate of registration and conditions of registration. Regulation 9 relates to the procedure where the registration is not granted, leading to the rejection of the application after giving an opportunity to the applicant to be heard. The applicant has right to appeal for reconsideration and SEBI shall reconsider the application and communicate its decision to the applicant in writing.

Regulation 11 imposes the duty on the applicant to pay the fees as prescribed. Non-payment of fees may result in suspension of the registration and the applicant shall cease to carry on the activity as a banker to the issue during the period of suspension.

GENERAL OBLIGATIONS AND RESPONSIBILITIES

Regulation 12 requires every banker to an issue to maintain the following records with respect to:

- (a) the number of applications received, the names of the investors, the dates on which the applications were received and the amounts so received from the investors;
- (b) the time within which the applications received from the investors were forwarded to the body corporate or registrar to an issue as the case may be;
- (c) the dates and amount of the refund monies paid to the investors;
- (d) dates, names and amount of dividend/interest warrant paid to the investors.

The Banker to an issue shall intimate to SEBI about the place where these documents are kept and shall preserve them for a minimum period of 3 years.

Regulation 13 requires the banker to inform SEBI as to the number of issues for which he was engaged as banker and certain other additional information regarding the monies received, the refunds made and the dividend/interest warrant paid.

Regulation 14 requires the banker to enter into an agreement with the body corporate for whom he is the banker to an issue with regard to the following matters:

- (a) the number of centres at which the application and the application monies of an issue of a body corporate will be collected from the investors;
- (b) the time within which the statements regarding the applications and the application monies received from the investors investing in an issue of a body corporate will be forwarded to the registrar to an issue of the body corporate, as the case may be;
- (c) the daily statement will be sent by the designated controlling branch of the bankers to the issue to the registrar to an issue indicating the number of body corporate and the amount of application money received.

Regulation 15 requires the banker to issue to inform SEBI about disciplinary action taken, if any by the RBI against him in relation to issue payment work. If as a result of such action the banker to issue is prohibited from carrying on the activities, the certificate shall be deemed to have been cancelled or suspended as the case may be.

CODE OF CONDUCT

Regulation 16 prescribes that every banker to an issue shall abide by the Code of Conduct as specified in Schedule III of the Regulations.

COMPLIANCE OFFICER

Regulation 16A provides that every banker to an issue is required to appoint a compliance officer responsible for monitoring the compliance of the Act, rules and regulations, notifications, guidelines, instructions etc. issued by SEBI or Central Government. He shall also be entrusted with the responsibility of redressal of investors' grievances. He is required to immediately and independently report to SEBI regarding any non-compliance observed by him.

PROCEDURE FOR INSPECTION

Chapter IV containing Regulation 17 to 22 deals with inspection of Banker to an Issue.

Regulation 17 and 18 authorise SEBI to request RBI to undertake inspection of the books of accounts, records and documents of the banker, to ensure their proper maintenance, and compliance with SEBI Act, Rules and Regulations, to investigate into the complaints received from investors, body corporates or any other person on any matter having a bearing on the activities of the banker as a banker to an issue and to investigate into any other matter referred by SEBI.

Regulation 19 lays down that RBI shall on receipt of the request from SEBI take appropriate steps to undertake inspection of Bankers to an Issue for such purposes as may be required by SEBI.

Regulation 20 requires that the banker shall offer all assistance and co-operation to RBI's inspecting officers to facilitate the inspection.

Regulation 21 stipulates that the RBI shall furnish to SEBI, copy of the inspection report along with copies of other relevant documents in support of the observations made by the inspecting authority.

ACTION ON INSPECTION OR INVESTIGATION REPORT

SEBI or the Chairman after consideration of inspection or investigation report may take such action as the SEBI or its chairman may deem fit and appropriate including action under Chapter V of SEBI (Intermediaries) Regulations, 2008.

PROCEDURE FOR ACTION IN CASE OF DEFAULT

Regulation 23 provides that banker to an issue who contravenes any of the provisions of the Act, rules or regulations framed thereunder, shall be dealt with in the manner provided under Chapter V of the SEBI (Intermediaries) Regulations, 2008.

DEBENTURE TRUSTEES

'Debenture Trustee' means a trustee of a trust deed for securing any issue of debentures of a body corporate. Debentures, Bonds and other hybrid instruments in most cases unless otherwise specified, carry securities for the investors unlike in the case of equity and preference shares. It is necessary that the company makes proper arrangements to extend assurances and comply with legal requirements in favour of the investors who are entitled to this type of security.

Intermediaries such as Trustees who are generally Banks and Financial Institutions render this service to the investors for a fee payable by the company. The issuing company has to complete the process of finalising and executing the trust deed or document and get it registered within the prescribed period and file the charge with the Registrar of Companies (ROC) in respect of the security offered.

Role and Functions include:

- Call for periodical reports from the body corporate, i.e., issuer of debentures.
- Take possession of trust property in accordance with the provisions of the trust deed.

- Enforce security in the interest of the debenture holders.
- Ensure on a continuous basis that the property charged to the debenture is available and adequate at all times to discharge the interest and principal amount payable in respect of the debentures and that such property is free from any other encumbrances except those which are specifically agreed with the debenture trustee.
- Exercise due diligence to ensure compliance by the body corporate with the provisions of the Companies Act, the listing agreement of the stock exchange or the trust deed.
- To take appropriate measures for protecting the interest of the debenture holders as soon as any breach of the trust deed or law comes to his notice.
- To ascertain that the debentures have been converted or redeemed in accordance with the provisions and conditions under which they are offered to the debenture holders.
- Inform the SEBI immediately of any breach of trust deed or provision of any law.
- Appoint a nominee director on the board of the body corporate when required.

SEBI (DEBENTURE TRUSTEES) REGULATIONS, 1993

These regulations were notified by SEBI effective from 29th December, 1993 in exercise of the powers conferred by Section 30 of SEBI Act, 1992 after previous approval of the Central Government.

Chapter I contains preliminary matters and definitions.

Chapter II consisting Regulations 3 to 12 deals with the procedure for registration of debenture trustees.

Regulation 3 stipulates that the application for registration shall be made in Form A. Schedule II of these regulation accompanied by a non-refundable application fee as prescribed in Regulation 4 authorises SEBI to call for and obtain further information from the applicant before granting the registration. The applicant or its principal officer may, if so required, appear before SEBI for personal representation. Regulation 5 stipulates that an application which is incomplete and does not conform to instructions shall be rejected after giving an opportunity to the applicant to remove such objections within time specified.

Regulation 6 lays down that SEBI shall take into account the following matters in considering the application, namely that the applicant:

- (1) has the necessary infrastructure like adequate office space, equipments, and manpower to effectively discharge his activities;
- (2) has any past experience as a debenture trustee or has in his employment minimum two persons who had the experience in matters which are relevant to a debenture trustee; or
- (3) any person, directly or indirectly connected with the applicant has not been granted registration by SEBI under the Act;
- (4) has in his employment at least one person who possesses the professional qualification in law from an institution recognised by the Government; or
- (5) any of its director or principal officer is or has at any time been convicted for any offence involving moral turpitude or has been found guilty of any economic offence and is a fit and proper person;
- (6) is a fit and proper person;
- (7) fulfills the capital adequacy requirements specified in Regulation 7A of these Regulations.

Regulation 7 lays down that to be a debenture trustee the applicant shall be a scheduled bank carrying on commercial activity, a public financial institution, an insurance company or a body corporate.

Regulation 7A of the Regulations provide that the capital adequacy requirement of debenture trustee shall not be less than the networth of ₹ 2 crore.

Regulations 8 and 9A deal with the procedure for registration and the renewal thereof, conditions of registration, time period for disposal of application and period of validity of certificate.

Regulation 10 lays down that if an applicant does not fulfill the requirements of Regulation 6 above, it may be rejected after giving reasonable opportunity to the applicant for being heard. The rejection shall be conveyed in writing by SEBI and the applicant may again apply for reconsideration of SEBI. After due reconsideration SEBI shall communicate its bindings in writing to the applicant.

Regulation 12 deal with non-payment of fees by the applicant. In the absence of a valid certificate the trustee shall cease to act as a debenture trustee.

RESPONSIBILITIES AND OBLIGATIONS OF DEBENTURE TRUSTEES

Chapter III containing Regulations 13 to 18 deals with this topic. Regulation 13 lays down that no debenture trustee who has been granted a certificate by SEBI shall act as debenture trustee unless he enters into a written agreement with the body corporate before the opening of the subscription list for issue of debentures and the agreement inter alia contains i) an undertaking by the body corporate to comply with all regulations / provisions of Companies Act, 2013, guidelines of other regulatory authorities in respect of allotment of debentures till redemption; and (ii) the time limit within which the security for the debentures shall be created or the agreement shall be executed in accordance with the Companies Act, 2013 or provisions as prescribed by any regulatory authority as applicable.

Regulation 13A stipulates that a person shall not be appointed as a debenture trustee, in case the debenture trustee, –

- (i) is an associate of the body corporate;
- (ii) beneficially holds shares in the company;
- (iii) is a promoter, director or key managerial personnel or any other officer or an employee of the company or its holding, subsidiary or associate company;
- (iv) is beneficially entitled to moneys which are to be paid by the company otherwise than as remuneration payable to the debenture trustee;
- (v) is indebted to the company, or its subsidiary or its holding or associate company or a subsidiary of such holding company;
- (vi) has furnished any guarantee in respect of the principal debts secured by the debentures or interest thereon;
- (vii) has any pecuniary relationship with the company amounting to 2% or more of its gross turnover or total income or 50 lakh or such higher amount as may be prescribed, whichever is lower, during the two immediately preceding financial years or during the current financial year;
- (viii) is relative of any promoter or any person who is in the employment of the company as a director or key managerial personnel; and
- (ix) is likely to have conflict of interest in any other manner.

However this requirement shall not be applicable in respect of debentures issued, wherever there is guarantee by the state / central government for the debentures issued.

Regulation 14 provides that every debenture trustee shall amongst other matters accept the trust deed which contains the matters specified in Section 71 of Companies Act, 2013 and Form No.SH-12 specified under the Companies (Share Capital and Debentures) Rules, 2014.

DUTIES OF DEBENTURE TRUSTEES

Regulation 15 casts the following duties on the debenture trustees:

- (1) satisfy itself that the prospectus or letter of offer does not contain any matter which is inconsistent with the terms of the issue of debentures or with the trust deed;
- (2) satisfy itself that the covenants in the trust deed are not prejudicial to the interest of the debenture holders;
- (3) call for periodical status/ performance reports from the issuer company within 7 days of the relevant board meeting or within 45 days of the respective quarter whichever is earlier;
- (4) communicate promptly to the debenture holders defaults, if any, with regard to payment of interest or redemption of debentures and action taken by the trustee therefor;
- (5) appoint a nominee director on the Board of the company in the event of:
 - two consecutive defaults in payment of interest to the debenture holders; or
 - default in creation of security for debentures; or
 - default in redemption of debentures.
- (6) ensure that the company does not commit any breach of the terms of issue of debentures or covenants of the trust deed and take such reasonable steps as may be necessary to remedy any such breach;
- (7) inform the debenture holders immediately of any breach of the terms of issue of debentures or covenants of the trust deed;
- (8) ensure the implementation of the conditions regarding creation of security for the debentures, if any, and debenture redemption reserve;
- (9) ensure that the assets of the company issuing debentures and of the guarantors, if any, are sufficient to discharge the interest and principal amount at all times and that such assets are free from any other encumbrances except those which are specifically agreed to by the debenture holders;
- (10) do such acts as are necessary in the event the security becomes enforceable;
- (11) call for reports on the utilization of funds raised by the issue of debentures;
- (12) take steps to convene a meeting of the holders of debentures as and when such meeting is required to be held;
- (13) ensure that the debentures have been converted or redeemed in accordance with the terms of the issue of debentures;
- (14) perform such acts as are necessary for the protection of the interest of the debenture holders and do all other acts as are necessary in order to resolve the grievances of the debenture holders;
- (15) take possession of trust property in accordance with the provisions of the trust deed;
- (16) to take appropriate measures for protecting the interest of the debenture holders as soon as any breach of the trust deed or law comes to his notice;
- (17) ascertain and satisfy itself that,-

- in case where the allotment letter has been issued and debenture certificate is to be issued after registration of charge, the debenture certificates have been dispatched by the body corporate to the debenture holders within 30 days of the registration of the charge with the Registrar of Companies;
 - debenture certificates have been dispatched to the debenture holders or debentures have been credited in the demat accounts of the debenture holders in accordance with the provisions of SEBI (Debenture Trustee) Regulations 1993, SEBI (Issue and Listing of Debt Securities) Regulations 2008, SEBI (Listing Obligations and Disclosure Requirements) Regulations 2015 and any other regulations issued by SEBI;
 - interest warrants for interest due on the debentures have been dispatched to the debenture holders on or before the due dates;
 - debenture holders have been paid the monies due to them on the date of redemption of the debentures;
- (18) inform the SEBI immediately of any breach of trust deed or provision of any law, which comes to the knowledge of the trustee.
- Explanation:* The communication to the debenture holders by the debenture trustee as mentioned in these regulations may be made by electronic media, press-release and placing notice on its website;
- (19) exercise due diligence to ensure compliance by the body corporate, with the provisions of the Companies Act, SEBI (Listing Obligations and Disclosure Requirement), Regulations, 2015, the listing agreement of the stock exchange or the trust deed or any other regulations issued by SEBI pertaining to debt issue;
- (20) In case where listed debt securities are secured by way of receivables/ book debts it shall obtain the following,-
- On Quarterly basis –
 - (a) Certificate from the Director / Managing Director of the issuer company certifying the value of the book debts / receivables;
 - (b) Certificate from an independent chartered accountant giving the value of book debts / receivables.
 - On Yearly basis- Certificate from the statutory auditor giving the value of book debts / receivables.
- (21) The debenture trustee shall –
- (a) obtain reports from the leading bank regarding the project.
 - (b) monitor utilization of funds raised in the issue.
 - (c) obtain a certificate from the issuer's statutory auditor.
 - (i) in respect of utilization of funds during the implementation period of the project; and
 - (ii) in the case of debentures issued for financing working capital at the end of accounting year.
- (22) A debenture trustee may call or cause to be called by the body corporate a meeting of all the debenture holders on –
- (a) a requisition in writing signed by at least one-tenth of the debentureholders in value for the time being outstanding.
 - (b) the happening of any event, which constitutes a default or which in the opinion of the debenture trustees affects the interest of the debentureholders.
- (23) No debenture trustee can relinquish its assignment in respect of the debenture issue of any body corporate, unless and until another debenture trustee is appointed in its place by the body corporate.

- (24) A debenture trustee is required to maintain the network requirements on a continuous basis. He is under an obligation to inform SEBI immediately in respect of any shortfall in the network. He is also not entitled to undertake new assignments until it restores the network to the level of specified requirement within the time specified by SEBI.
- (25) Debenture trustee may inspect books of accounts, records, registers of the body corporate and the trust property to the extent necessary for discharging its obligations.
- (26) Supervise the implementation of the conditions regarding creation of security for the debentures and debenture redemption reserve, wherever applicable.

CODE OF CONDUCT

Regulation 16 requires that every debenture trustee shall abide by the code of conduct as specified in Schedule III to the Regulations.

MAINTENANCE OF RECORDS

Regulations 17 and 18 deal with maintenance of books of accounts, records and documents relating to trusteeship functions for a period of not less than five financial years from the date of redemption of debentures. Every debenture trustee would inform SEBI about the place where the books of accounts, records and documents are maintained and furnish various information to SEBI.

APPOINTMENT OF COMPLIANCE OFFICER

Regulation 17A provides that every debenture trustee is required to appoint a compliance officer responsible for monitoring the compliance of the Act, rules and regulations, notifications, guidelines, instructions etc. issued by SEBI or Central Government. He is also responsible for redressal of investor grievances. The compliance officer is under an obligation to immediately and independently report to SEBI any non-compliance observed by him. He would also report any non-compliance of the requirements specified in the listing agreement with respect to debenture issues and debentureholders, by the body corporate to SEBI. The compliance officer so appointed shall obtain certification in terms of SEBI (Certification of Associated Persons in the Securities Markets) Regulations, 2007 or as may be specified by SEBI.

INFORMATION TO SEBI

Regulation 18 provides that Debenture trustee is required to submit the following information and documents to SEBI, as and when SEBI may require –

- (a) The number and nature of the grievances of the debentureholders received and resolved.
- (b) Copies of the trust deed.
- (c) Non-Payment or delayed payment of interest to debentureholders, if any, in respect of each issue of debentures of a body corporate.
- (d) Details of despatch and transfer of debenture certificates giving therein the dates, modes etc.
- (e) Any other particular or document which is relevant to debenture trustee.

ACTION ON INSPECTION OR INVESTIGATION REPORT

Chapter IV consisting of Regulation 19 to 24 deals with inspection and disciplinary proceedings.

SEBI or chairman, may after consideration of inspection or investigation report take such action as the SEBI or chairman may deem fit and appropriate including action under Chapter V of SEBI (Intermediaries) Regulations, 2008.

PROCEDURE FOR ACTION IN CASE OF DEFAULT

Regulation 25 of Chapter V lays down that a debenture trustee would be dealt with in the manner provided under Chapter V of SEBI (Intermediaries) Regulations, 2008, if he fails to comply with the conditions of registration, contravenes the provisions of SEBI Act/Companies Act, Rules and Regulations.

SYNDICATE MEMBERS

Syndicate Member means an intermediary registered with SEBI and who is permitted to carry on the activity as an underwriter. The Book Runner(s) may appoint those intermediaries who are registered with the SEBI and who are permitted to carry on activity as an 'Underwriter' as syndicate members. The syndicate members are mainly appointed to collect the entire bid forms in a book built issue.

Syndicate Member/Broker is a member of the Stock Exchange to whom the investor has to submit the IPO Bid/ Application form. The Syndicate Member / Broker receives the bid and uploads the same on the electronic book of the stock exchange. The Syndicate Member/Broker, then submits the bid with cheque to the bankers. In case of online application, the Syndicate Member/Broker generates the electronic application form and submits the same to the registrar with proof of having paid the bid amount.

STOCK BROKERS & SUB-BROKER

Stock-broker means a member of stock exchange and they are the intermediaries who are allowed to trade in securities on the exchange of which they are members. They buy and sell on their own behalf as well as on behalf of their clients.

A sub-broker is one who works along with the main broker and is not directly registered with the stock exchange as a member. Sub-broker means any person not being a member of stock exchange who acts on behalf of a stock broker as an agent or otherwise for assisting the investors in buying, selling or dealing in securities through such stock brokers.

A stock broker plays a very important role in the secondary market helping both the seller and the buyer of the securities to enter into a transaction. The buyer and seller may be either a broker or a client. The transaction entered cannot be annulled except in the case of fraud, willful misrepresentation or upon prima-facie evidence of a material mistake in the transaction, in the judgement of the existing authorities. If a member of the stock exchange (broker) has orders to buy and to sell the same kind of securities, he may complete the transaction between his clients concerned.

When executing an order, the stock broker may on behalf of his client buy or sell securities from his own account i.e. as principal or act as an agent. For each transaction he has to issue necessary contract note indicating whether the transaction has been entered into by him as a principal or as an agent for another. While buying or selling securities as a principal, the stock broker has to obtain the consent of his client and the prices charged should be fair and justified by the conditions of the market.

SEBI (STOCK BROKERS AND SUB-BROKERS) REGULATIONS, 1992

SEBI (Stock Brokers & Sub-Brokers) Regulations, 1992 were notified by SEBI in exercise of the powers conferred by section 30 of SEBI Act, 1992 and came into effect on 23rd October, 1992.

Chapter II of the Regulations contains Regulation 3 to 10 which deals with registration of Stock Brokers. An application by a stock broker for grant of a certificate of registration shall be made through the Stock exchange, of which he is admitted as a member. The stock exchange shall forward the application form to SEBI as early as possible but not later than 30 days from the date of its receipt. SEBI may require the applicant to furnish such further information or clarifications regarding the dealings in securities and related matters to consider the

application for granting a certificate of registration. The applicant or its principal officer shall, if so required, appear before SEBI for personal representation.

SEBI shall take into account the following aspects before granting a certificate:

- (a) whether the applicant is eligible to be admitted as a member of a stock exchange;
- (b) whether he has the necessary infrastructure like adequate office space, equipment and manpower to effectively discharge his activities;
- (c) whether he has any past experience in the business of buying, selling or dealing in securities;
- (d) whether he was subjected to disciplinary proceedings under the rules, regulations and bye-laws of a stock exchange with respect to his business as a stock broker involving either himself or any of his partners, directors or employees; and
- (e) whether he is a fit and proper person.
- (f) has any financial liability which is due and payable in terms of the Act, the Securities Contracts (Regulation) Act, 1956 or rules and regulations thereunder;
- (g) has obtained certification in terms of SEBI (Certification of Associated Persons in the Securities Markets) Regulations, 2007 or as may be specified by SEBI;
- (h) satisfies the minimum net worth and deposit requirements as specified in Schedule VI, for the segment for which membership or approval is sought.

Regulation 6 lays down that the SEBI may, after consideration of the application of registration and on being satisfied that the applicant has complied with the conditions laid down in regulation 5 grant a certificate of registration in Form D to the stock-broker, and send intimation to that effect to the stock exchange(s) of which it is a member.

Regulation 7 stipulates that where an application for grant does not fulfil the requirements as prescribed in regulations, SEBI may reject the application after giving a reasonable opportunity of being heard. The refusal to grant the registration certificate shall be communicated by the SEBI within 30 days of such refusal to the applicant and to the concerned stock exchange stating therein the grounds on which the application has been rejected. An applicant aggrieved by the decision of SEBI, may apply within a period of 30 days from the date of receipt of such intimation, to the SEBI for reconsideration of its decision. SEBI shall reconsider an application and communicate its decision as soon as possible in writing to the applicant and to the concerned stock exchange.

REJECTION OF APPLICATION OF BROKERS

Regulation 8 lays down that every applicant eligible for grant of a certificate of registration shall pay such fees and in such manner as specified in Schedule III or Schedule V as the case may be. However, SEBI may on sufficient cause being shown, permit the stock broker to pay such fees at any time before the expiry of 6 months from the date on which such fees become due.

Regulation 9 lays down the following conditions for registration:-

- (a) he shall abide by the rules, regulations and bye-laws of the stock exchange which are applicable to him;
- (b) he shall pay fees charged by SEBI in the manner provided in these regulations;
- (c) he shall take adequate steps for redressal of grievances, of the investors within one month of the date of receipt of the complaint and keep the SEBI informed about the number, nature and other particulars of the complaints received from such investors; and

- (d) the stock broker holds the membership of any stock exchange;
- (e) where the stock broker proposes change in control, he shall obtain prior approval of the SEBI for continuing to act as such after the change
- (f) he shall at all times abide by the Code of Conduct as specified in Schedule II; and
- (g) he shall at all times maintain the minimum net worth as specified in Schedule VI.

Regulation 10 deals with approval for operation in other stock exchange(s) or segment(s) of stock exchange. A stock broker registered with SEBI, who desires to operate in any segment(s) of the stock exchange of which it holds a membership, shall apply to the concerned stock exchange, in the manner specified by SEBI. A clearing member registered with SEBI, who desires to operate in any segment(s) of the stock exchange which has promoted the clearing corporation, of which he is a member, shall apply to the concerned stock exchange in the manner specified by SEBI. On receipt of an application, the stock exchange shall, on being satisfied with the compliance of provision of the regulations and other relevant eligibility requirements specified by SEBI, grant approval for operation in any segment(s) and shall inform the SEBI about such grant of approval.

REGISTRATION OF CLEARING MEMBERS

Chapter II-A consisting of Regulations 10A to 10 F deals with registration of clearing members. Regulation 10A on procedure for application for registration requires that no person shall act as a clearing member, unless he obtains a certificate of registration from SEBI.

However, no separate registration shall be required for a stock broker registered with SEBI to act as a clearing member in a clearing corporation of which he is admitted as a member, subject to grant of approval by the concerned clearing corporation. An application for grant of a certificate of registration as clearing member shall be submitted to SEBI in Form AD of Schedule I through the Clearing Corporation of which he is admitted as a member. The Clearing Corporation shall forward the application form to SEBI as early as possible, but not later than 30 days from the date of its receipt.

Regulation 10B provides the provisions of Chapter II shall be applicable mutatis mutandis to registration of a clearing member, except as otherwise provided."

Regulation 10C provides that every applicant eligible for grant of a certificate of registration as a clearing member shall pay such fees and in such manner as specified in Schedule III or Schedule V as the case maybe. SEBI may on sufficient cause being shown permit the clearing member to pay such fees at any time before the expiry of 6 months from the date on which such fees become due.

Regulation 10D deals with approval for operation in other clearing corporation(s) or segment(s) of clearing corporation. A clearing member registered with SEBI, who desires to operate in any other clearing corporation or any other segment(s) of the Clearing Corporation of which it holds a membership, shall apply to the concerned clearing corporation in the manner specified by SEBI. A stock broker registered with SEBI, who desires to operate in any clearing corporation or any segment(s) of the clearing corporation, shall apply to the concerned clearing corporation in the manner specified by SEBI. On receipt of an application, the clearing corporation shall, on being satisfied with the compliance of provisions of the regulations and other relevant eligibility requirements specified by SEBI, grant approval to operate in that clearing corporation or segment(s) thereof, and shall inform SEBI about such grant of approval.

Regulation 10E deals with Clearing Corporation for commodity derivatives. For the purpose of this Chapter and in respect of clearing and settlement of trades in commodity derivatives, the word clearing corporation, wherever appearing, shall refer to a commodity derivatives exchange till such time a separate clearing corporation is established to undertake the activity of clearing and settlement of trades in commodity derivatives.

REGISTRATION OF SUB-BROKERS

Chapter III containing Regulations 11 to 16 deal with registration of sub-brokers. A sub-broker cannot act as such unless he holds a certificate granted by SEBI. Where a sub-broker merely changes his affiliation from one stock broker to another stock broker being a member of the same stock exchange. There is no requirement of obtaining fresh certificate. Again there is no need of obtaining fresh certificate where a registered stock broker is affiliated to stock broker who is eligible to trade on SME platform.

Regulation 11A lays down that an application by a sub-broker for the grant of certificate shall be made in Form-B. Such application from the sub-broker applicant shall be accompanied by a recommendation letter in Form-C from a stock broker of a recognised stock exchange with whom the former is to be affiliated along with two references including one from his banker. The application form shall be submitted to the stock exchange of which the stock broker with whom he is to be affiliated is a member.

The stock exchange on receipt of an application shall verify the information contained therein and shall also certify that the applicant is eligible for registration as per criteria specified below:

- (1) In the case of an individual:
 - (a) the applicant is not less than 21 years of age;
 - (b) the applicant has not been convicted of any offence involving fraud or dishonesty;
 - (c) the applicant has at least passed 12th standard equivalent examination from an Institution recognised by the Government. However, SEBI may relax this criterion on merits having regard to the applicant's experience;
 - (d) the applicant is a fit and proper person.
- (2) In the case of partnership firm or a body corporate, the partners or directors as the case may be shall comply with the requirements stated above. It is also to be assessed whether the applicant has necessary infrastructure like adequate office space, equipment and manpower to effectively discharge his activities. The applicant should be person recognised by the stock exchange as a sub-broker affiliated to a member broker of the stock exchange.

The stock exchange shall forward the application form of such applicants, alongwith recommendation letter issued by the stock broker with whom he affiliated alongwith a recognition letter issued by the stock exchange to SEBI within 30 days from the date of its receipt.

SEBI on being satisfied that the sub-broker is eligible, shall grant a certificate in Form-E to the sub-broker and send an intimation to that effect to the stock exchange or exchanges as the case may be. SEBI may grant a certificate of registration to the applicant subject to the terms and conditions as laid down by SEBI in Regulation 12A.

Regulation 12A lays down the conditions of registration. Any registration granted by SEBI shall be subject to the following conditions: –

- (a) he shall abide by the rules, regulations and bye-laws of the stock exchange which are applicable to him;
- (b) he shall pay fees charged by SEBI;
- (c) he shall take adequate steps for redressal of grievances, of the investors within one month of the date of receipt of the complaint and keep SEBI informed about the number, nature and other particulars of the complaints received from such investors; and
- (d) he is authorized in writing by a stock-broker being a member of a stock exchange for affiliating himself in buying, selling or dealing in securities.

Where an application for grant of a certificate does not fulfil the requirements mentioned in Regulation 11A, SEBI may reject the application after giving a reasonable opportunity of being heard. The refusal to grant the certificate shall be communicated by SEBI within 30 days of such refusal to the concerned stock exchange and to the applicant in writing stating therein the grounds on which the application has been rejected. An applicant being aggrieved by the decision of SEBI may, within a period of 30 days from the date of receipt of such intimation apply to SEBI for reconsideration of the decision.

SEBI shall reconsider an application made and communicate its decision to the applicant in writing and to the concerned stock exchange as soon as possible.

A person whose application for grant of a certificate has been refused by SEBI shall, on and from the date of communication of refusal cease to carry on any activity as a sub-broker. The sub-broker has the following general obligations:

- (a) pay the fees as per Schedule III;
- (b) abide by the Code of Conduct specified in Schedule II;
- (c) enter into an agreement with the stock broker for specifying the scope of his authority and responsibilities;
- (d) comply with the rules, regulations and bye laws of the stock exchange;
- (e) not be affiliated to more than one stock broker of one stock exchange.

The sub-broker shall keep and maintain the books and documents specified in the Regulations.

No director of a stock broker can act as a sub-broker to the same stock broker.

The general obligations and responsibilities, procedure for inspection and for taking action in case of default shall be the same for both stock brokers and sub-brokers.

REGISTRATION OF TRADING AND CLEARING MEMBERS

Chapter IIIA consisting of Regulation 16A to 16I deals with registration of trading and clearing members. Regulation 16A on the procedure for application for registration requires that an application for grant of certificate of registration by a trading member of a derivatives exchange or derivatives segment of a stock exchange shall be made in Form-AA of Schedule-I, through the concerned derivatives exchange or derivatives segment of a stock exchange of which he is a member. Similarly an application for grant of certificate of registration by a clearing member or self clearing member of the clearing corporation or clearing house of a derivatives exchange or derivatives segment of a stock exchange shall be made in Form-AA of Schedule-I, through the concerned clearing corporation or clearing house of which is he a member. However, a trading member who also seeks to act as a clearing member or self clearing member shall make separate applications for each activity. The concerned exchange shall forward the application to SEBI as early as possible but not later than 30 days from the date of its receipt.

SEBI may require the applicant or the concerned stock exchange or segment or clearing house or corporation to furnish such other information or clarification regarding the trading and settlement in derivatives and matters connected thereto, to consider the application for grant of a certificate. The applicant or its principal officer, if so required shall appear before SEBI for personal representation.

SEBI shall take into account the following aspects while considering the application, namely –

1. whether the applicant is eligible to be admitted as a trading member or a clearing member as the case may be;

2. whether the applicant has the necessary infrastructure like adequate office space, equipment and man power to effectively undertake his activities; and
3. whether he is/was subjected to disciplinary procedures under the rules, regulations and bye-laws of any stock exchange with respect to his business, involving either himself or any of his partners, directors or employees;
4. whether the applicant has any financial liability which is due and payable to SEBI.

The applicant shall also have a net worth as may be specified from time to time and the approved user and sales personnel of the trading member shall have passed a certification programme approved by SEBI. An applicant who desires to act as a clearing member shall also have a minimum net worth of ₹ 300 lakhs and shall deposit at least a sum of ₹ 50 lakhs or higher amount with a clearing corporation or a clearing house of the derivatives exchange or derivatives segment in the form specified from time to time. An applicant who derives to act as a self clearing member, in addition shall comply with the requirement of minimum networth of ₹ 100 lakhs and shall deposit at least a sum of ₹ 50 lacs or higher amount with the clearing corporation or clearing house of the derivatives exchange or derivatives segment in the form specified from time to time.

Net worth in this context shall mean paid up capital plus free reserves and other securities approved by SEBI from time to time (but does not include fixed assets, pledged securities, value of members card, non allowable securities which are unlisted, bad deliveries, doubtful dates and advances of more than three months and debt/ advances given to the associate persons of the members), prepaid expenses, losses, intangible assets and 30% value of marketable securities.

REGISTRATION PROCEDURE FOR TRADING AND CLEARING MEMBER

Regulation 16I lays down that on being satisfied that the applicant is eligible, SEBI shall grant a certificate in Form-DA of Schedule-I to the applicant and send an intimation to that effect to the derivative segment of the stock exchange or derivatives exchange or clearing corporation or clearing house as the case may be. Where an application does not fulfil the requirements, SEBI may reject the application after giving a reasonable opportunity to the applicant of being heard. The refusal to grant such certificate shall be communicated by SEBI within 30 days of such refusal to the concerned segment of stock exchange or clearing corporation or clearing house and to the applicant stating therein the grounds on which the application has been rejected. If aggrieved by the decision of SEBI as referred to above, the applicant may apply within a period of 30 days from the date of receipt of such information to SEBI for reconsideration of its decision. SEBI shall reconsider the application and communicate its decision as soon as possible in writing to the applicant and to the concerned segment of stock exchange or clearing house or corporation.

If certificate of registration is refused to an applicant, then he shall not from the date of receipt of SEBI's letter of rejection, deal in or settle the derivatives contracts as a member of the derivatives exchange, segment, clearing corporation or clearing house. Every applicant eligible for grant of certificate as a trading or clearing member or self clearing member, shall pay such fee as may be specified. If the fee is not paid, SEBI may suspend or cancel the registration after giving an opportunity of being heard where upon the trading and clearing member or self-clearing member shall cease to deal in and settle the derivatives contract.

REGISTRATION OF TRADING AND CLEARING MEMBERS OF CURRENCY DERIVATIVES SEGMENT

Chapter IIIB containing Regulation 16J to 16R deals with registration of trading, clearing member and self-clearing member of currency derivative segment. Regulation 16J provide that the application for grant of certificate of registration by a trading member of currency derivatives segment of a stock exchange shall be made in Form AB of Schedule I, through the concerned currency derivatives segment of a stock exchange of which he is a

member. An application for grant of certificate of registration by a clearing member or self-clearing member of the clearing corporation or clearing house of currency derivatives segment of a stock exchange, shall be made in Form AB of Schedule I, through the concerned clearing corporation or clearing house of which he is a member: However, a trading member who also seeks to act as a clearing member or self-clearing member shall make separate applications for each activity in Form AB of Schedule I. The currency derivatives segment or clearing house or corporation, as the case may be, shall forward the application to SEBI as early as possible but not later than thirty days from the date of its receipt.

Regulation 16K provided that SEBI may require the applicant or the concerned stock exchange or segment or clearing house or corporation to furnish such other information or clarifications, regarding the trading and settlement in currency derivatives and matters connected thereto, to consider the application for grant of a certificate. The applicant or its principal officer shall, if so required, appear before SEBI for personal representation.

Regulation 16L lays down that SEBI shall take into account for considering the grant of a certificate all matters relating to dealing and settlement in currency derivatives and in particular the following, namely, whether the applicant –

- (a) is eligible to be admitted as a trading member or a clearing member or self-clearing member
- (b) has the necessary infrastructure like adequate office place, equipment and man-power to effectively undertake his activities;
- (c) is subjected to disciplinary proceedings under the rules, regulations and bye-laws of any stock exchange with respect to his business involving either himself or any of his partners, directors or employees;
- (d) has any financial liability which is due and payable to SEBI under these regulations.

An applicant shall also have a net worth of ₹ 1 Crore and shall ensure that its approved user and sales personnel have passed a certification programme approved by SEBI. An applicant who desires to act as a clearing member or self-clearing member shall have a minimum net worth of ₹ 10 crore and shall deposit at least a sum of ₹ 50 lacs or higher amount with the clearing corporation or clearing house of the currency derivatives segment in the form specified from time to time.

REGISTRATION PROCEDURE

Regulation 16M requires that on being satisfied that the applicant is eligible, SEBI shall grant a certificate in Form DB of Schedule I, to the applicant and send an intimation to that effect to the currency derivatives segment of the stock exchange or clearing corporation or clearing house, as the case may be. Regulation 16N provides that where an application for the grant of a certificate does not fulfill the requirements SEBI may reject the application of the applicant after giving a reasonable opportunity of being heard. The refusal to grant the certificate of registration shall be communicated by SEBI within 30 days of such refusal to the currency derivatives segment of the stock exchange, or clearing house or corporation and to the applicant stating therein the grounds on which the application has been rejected. An applicant may, if aggrieved by the decision of SEBI as referred to above, the applicant may apply within a period of thirty days from the date of receipt of such information to SEBI for reconsideration of its decision. SEBI shall reconsider an application made and communicate its decision as soon as possible in writing to the applicant and to the currency derivatives segment of the stock exchange or clearing house or corporation.

Regulation 16O lays down that an applicant, whose application for the grant of a certificate of registration has been refused by SEBI shall not on and from the date of receipt of the communication deal in or settle the currency derivatives contracts as a member of the currency derivatives segment of the stock exchange or clearing corporation or clearing house.

CODE OF CONDUCT

Regulation 16Q requires the code of conduct specified for the stock broker as stipulated in Schedule-II shall be applicable *mutatis mutandis* to the trading member, clearing member and self-clearing member and such members shall at all times abide by the same. The trading member shall obtain details of the prospective clients in “know your client” format as specified by SEBI before executing an order on behalf of such client. The trading member shall mandatorily furnish “risk disclosure document” disclosing the risk inherent in trading in derivatives to the prospective clients in the form specified. The trading or clearing member or self-clearing member shall deposit a margin money or any other deposit and shall maintain position or exposure limit as specified by SEBI or the concerned exchange or segment or clearing corporation or clearing house from time to time.

GENERAL OBLIGATIONS AND RESPONSIBILITIES

Chapter IV containing Regulations 17 and 18 deal with the general obligations and responsibilities of stock brokers. It lays down that every stock broker shall keep and maintain books of accounts, records and documents namely – Register of Transactions (Sauda book); clients ledger; general ledger; journals; cash book; bank pass book; documents, register including particulars of securities received and delivered in physical form and the statement of account and other records relating to receipt and delivery of securities provided by the depository participants in respect of dematerialised securities, members contract books showing details of all contracts entered into by him with other members of the same exchange or counterfoils or duplicates of memos of confirmation issued to such other members; counterfoils or duplicates of contract notes issued to clients; written consents of clients in respect of contracts entered into as principals; margin deposit book; registers of accounts of sub-brokers; an agreement with sub-broker specifying scope of authority, and responsibilities of the stock brokers as well as sub-brokers and client account opening Form in the format as specified by SEBI.

Every stock broker shall intimate to SEBI the place where the books of accounts, records and documents are maintained. He shall, after the close of each accounting period, furnish to SEBI if so required, as soon as possible but not later than 6 months from the close of the said period, a copy of the audited balance sheet and profit and loss account for the said accounting period.

If this is not possible, the stock broker shall keep SEBI informed of the same together with the reasons for the delay and the period of time by which such documents would be furnished to SEBI. Every stock broker shall preserve the books of accounts and other records for a minimum period of 5 years.

The stock broker shall not deal with any person as sub-broker unless such person has been granted certificate of registration by SEBI.

COMPLIANCE OFFICER

Regulation 18A requires every stock broker to appoint a compliance officer who shall be responsible for monitoring the compliance of the Act, rules and regulations, notifications, guidelines, instructions etc. issued by SEBI or Central Government and for redressal of investors’ grievances. Compliance officer shall immediately and independently report to SEBI any non-compliance observed by him.

Regulation 18B provides that the stock broker shall not deal with any person as a sub-broker unless such person has been granted certificate of registration by SEBI.

PROCEDURE FOR INSPECTION OF STOCK BROKERS’ OFFICES

Regulations 19 to 24 provides for procedure for inspection. It is provided that where it appears necessary to SEBI, it may appoint one or more persons as inspecting authority to undertake inspection of the books of accounts other records and documents of the stock brokers:

- (a) to ensure that the books of account and other books are being maintained in the manner required,

- (b) that the provisions of the Act, rules and regulations as well as the provisions of the Securities Contracts (Regulation) Act, 1956 and the rules made thereunder are being complied with,
- (c) to investigate into the complaints received from investors, other stock brokers, sub-brokers or any other person on any other matter having a bearing on the activities of the stock brokers, and
- (d) to investigate suo motu in the interest of securities business or investors interest into the affairs of the stock broker.

Before undertaking inspection, SEBI shall give a reasonable notice to the stock broker. However, if SEBI is satisfied that in the interest of the investors or in public interest, no such notice should be given, it may by an order in writing, direct that the inspection be taken up without such notice to the stock broker. On being empowered by SEBI, the inspecting authority shall undertake the inspection and the stock broker concerned shall be bound to discharge his obligations to facilitate and co-operate for the conduct of inspection by the said authority.

It shall be the duty of every director, proprietor, partner, officer and employee of the stock broker who is being inspected, to produce to the inspecting authority such books, accounts and other documents in his custody or control and furnish him with the statements and information relating to the transactions in securities market within such time as the inspecting authority may require.

The stock broker shall allow the inspecting authority to have reasonable access to the premises occupied by such stock broker or by any other person on his behalf and also extend reasonable facility for examining any books, records, documents and computer data in the possession of the stock broker or any other person and also provide copies of documents or other materials which in the opinion of the inspecting authority are relevant. The said authority in the course of inspection shall be entitled to examine or record statements of any member, director, partner, proprietor and employee of the stock broker. It shall be duty of every director, proprietor, partner, officer and employee of stock broker to give the said authority all assistance in connection with the inspection, which the stock broker may be reasonably expected to give.

The inspecting authority shall as soon as possible submit an inspection report to SEBI who shall after consideration of inspection or investigation report take such action as it may deem fits and appropriate including action under Chapter V of SEBI (Intermediaries) Regulations, 2008.

SEBI is also empowered to appoint a qualified auditor to investigate into the books of accounts or the affairs of the stock broker. The auditor so appointed shall have the same powers of the inspecting authority as enumerated above and the obligations of the stock broker as detailed above shall be applicable to the investigation.

PROCEDURE FOR ACTION IN CASE OF DEFAULT

A stock broker or a sub-broker who contravenes any of the provisions of the Act, rules or regulations framed thereunder shall be liable for any one or more of the following actions—

- (i) Monetary penalty under Chapter VIA of the Act.
- (ii) Penalties as specified under Chapter V of SEBI (Intermediaries) Regulations, 2008 including suspension or cancellation of certificate of registration as a stock broker or a sub-broker.
- (iii) Prosecution under Section 24 of the Act.

LIABILITY FOR MONETARY PENALTY

A stock broker or a sub-broker shall be liable for monetary penalty in respect of the following violations, namely –

- (i) Failure to file any return or report with SEBI.
- (ii) Failure to furnish any information, books or other documents within 15 days of issue of notice by SEBI.
- (iii) Failure to maintain books of account or record as per the Act, rules or regulations framed thereunder.
- (iv) Failure to redress the grievances of investors within 30 days of receipts of notice from SEBI.
- (v) Failure to issue contract notes in the form and manner specified by the Stock Exchange of which such broker is a member.
- (vi) Failure to deliver any security or make payment of the amount due to the investor within 48 hours of the settlement of trade unless the client has agreed in writing otherwise.
- (vii) Charging of brokerage which is in excess of brokerage specified in the regulations or the bye-laws of the stock exchange.
- (viii) Dealing in securities of a body corporate listed on any stock exchange on his own behalf or on behalf of any other person on the basis of any unpublished price sensitive information.
- (ix) Procuring or communicating any unpublished price sensitive information except as required in the ordinary course of business or under any law.
- (x) Counselling any person to deal in securities of any body corporate on the basis of unpublished price sensitive information.
- (xi) Indulging in fraudulent and unfair trade practices relating to securities.
- (xii) Failure to maintain client opening form.
- (xiii) Failure to segregate his own funds or securities from the client's funds or securities or using the securities or funds of the client for his own purpose or for purpose of any other client.
- (xiv) Acting as an unregistered sub-broker or dealing with unregistered sub-brokers.
- (xv) Failure to comply with directions issued by SEBI under the Act or the regulations framed thereunder.
- (xvi) Failure to exercise due skill, care and diligence.
- (xvii) Failure to obtain prior approval of SEBI in case of change in control of stock broker.
- (xviii) Failure to satisfy the net worth or capital adequacy norms, if any, specified by SEBI.
- (xix) Extending use of trading terminal or any unauthorized person or place.
- (xx) Violations for which no separate penalty has been provided under these regulations.

LIABILITY FOR ACTION UNDER THE ENQUIRY PROCEEDING

A stock broker or a sub-broker shall be liable for any action as specified in SEBI (Intermediaries) Regulations, 2008 including suspension or cancellation of his certificate of registration as a stock broker or a sub-broker, as the case may be, if he –

- (i) ceases to be a member of a stock exchange; or
- (ii) has been declared defaulter by a stock exchange and not re-admitted as a member within a period of six months; or

- (iii) surrender his certificate of registration to SEBI; or
- (iv) has been found to be not a fit and proper person by SEBI under these or any other regulations; or
- (v) has been declared insolvent or order for winding up has been passed in the case of a broker or sub-broker being a company registered under the Companies Act, 1956 (now Companies, 2013); or
- (vi) or any of the partners or any whole-time director in case a broker or sub-broker is a company registered under the Companies Act, 1956 (now Companies, 2013) has been convicted by a court of competent jurisdiction for an offence involving moral turpitude; or
- (vii) fails to pay fee as per Schedule III of these regulations; or
- (viii) fails to comply with the rules, regulations and bye-laws of the stock exchange of which he is a member; or
- (ix) fails to co-operate with the inspecting or investigating authority; or
- (x) fails to abide by any award of the Ombudsman or decision of SEBI under the SEBI (Ombudsman) Regulations, 2003; or
- (xi) fails to pay the penalty imposed by the Adjudicating Officer; or
- (xii) indulges in market manipulation of securities or index; or
- (xiii) indulges in insider trading in violation of SEBI (Prohibition of Insider Trading) Regulations, 1992; or
- (xiv) violates SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 2003; or
- (xv) commits violation of any of the provisions for which monetary penalty or other penalties could be imposed; or
- (xvi) fails to comply with the circulars issued by SEBI; or
- (xvii) commits violations specified in Regulation 26 which in the opinion of SEBI are of a grievous nature.

LIABILITY FOR PROSECUTION

A stock broker or a sub-broker shall be liable for prosecution under Section 24 of the SEBI Act for any of the following violations, namely –

- (i) Dealing in securities without obtaining certificate of registration from SEBI as a stock broker or a sub-broker.
- (ii) Dealing in securities or providing trading floor or assisting in trading outside the recognized stock exchange in violation of provisions of the Securities Contract (Regulation) Act, 1956 or rules made or notifications issued thereunder.
- (iii) Market manipulation of securities or index.
- (iv) Indulging in insider trading in violation of SEBI (Prohibition of Insider Trading) Regulations, 1992.
- (v) Violating SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 2003.
- (vi) Failure without reasonable cause –
 - (a) to produce to the investigating authority or any person authorized by him in this behalf, any books, registers, records or other documents which are in his custody or power; or
 - (b) to appear before the investigating authority personally or to answer any question which is put to him by the investigating authority; or

- (c) to sign the notes of any examination taken down by the investigating authority.
- (vii) Failure to pay penalty imposed by the adjudicating officer or failure to comply with any of his directions or orders.

A CASE STUDY ON FRAUDULENT DEALINGS

Bishwanath Murlidhar Jhunjunwala v. SEBI

SEBI noticed a spurt in the volume in the trading of the scrip of Snowcem India Ltd. (SIL), both at NSE and BSE. Though the scrip was not very liquid, it was observed that during June 1999 to August 1999, price of the scrip ranged between ₹55 to ₹127. The Appellant, a stock broker of BSE himself was found to have registered himself as a client with a broker of NSE and placed orders in large quantities in the scrip of SIL to the tune of 2,87,400 shares which amounted to 5.59 per cent of the total volume traded at NSE between June 1999 and August 1999. Orders placed by the Appellant were matched with those orders placed by Kosha Investment Ltd. (KIL). Further, the Appellant had not traded in his own account at BSE. The conduct of the Appellant was in violation of Regulation 4 (a), (b) and (d) of SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 2003 in view of which he was prohibited from accessing capital market for a period of 2 years. Upholding the impugned order in its totality, the Hon'ble SAT noted that, "It is a fact that the persons who operate in the market are required to maintain high standards of integrity, promptitude and fairness in the conduct of business dealings.

CERTIFICATION BY PRACTISING COMPANY SECRETARY

1. Internal Audit for Stock Brokers/Trading Members/ Clearing Members

SEBI has authorized the Practising Company Secretary to carry out complete internal audit of stock brokers/trading members/clearing members on a half yearly basis. The circular states that stock brokers/trading members/clearing members shall carry out complete internal audit on a half yearly basis by chartered accountants, company secretaries or cost and management accountants who are in practice and who do not have any conflict of interest. The scope of such audit covers, inter alia, the existence, scope and efficiency of the internal control system, compliance with the provisions of the SEBI Act, 1992, Securities Contracts (Regulation) Act 1956, SEBI (Stock Brokers and Sub-Brokers) Regulations, 1992, circulars issued by SEBI, agreements, KYC requirements, Bye Laws of the Exchanges, data security and insurance in respect of the operations of stock brokers/clearing members. The objective of internal audit is –

- (i) to ensure that the books of account, records (including telephone records and electronic records) and documents are being maintained in the manner required under SEBI Act, 1992, SCR Act, 1956 and SEBI (Stock brokers and Sub-brokers) Regulations, 1992.
- (ii) to ascertain as to whether adequate internal control systems, procedures and safeguards have been established and are being followed by the intermediary to fulfill its obligations within the scope of the audit.
- (iii) to ascertain as to whether any circumstances exist which would render the intermediary unfit or ineligible.
- (iv) to ascertain whether the provisions of the securities laws and the directions or circulars issued thereunder are being complied with.
- (v) to ascertain whether the provision of stock exchange bye-laws, notices, circulars, instructions or orders issued by stock exchanges are being complied with.
- (vi) to inquire into the complaints received from investors, clients, other market participants or any other person on any matter having a bearing on the activities of the stock broker.

PORTFOLIO MANAGERS

Portfolio manager means any person who pursuant to contract or arrangement with the client, advises or directs or undertakes on behalf of the client (whether as a discretionary portfolio manager or otherwise) the management or administration of a portfolio of securities or the funds of the clients as the case may be. “Discretionary portfolio manager” is defined as one who exercises or may exercise, under a contract relating to portfolio management, any degree of discretion as to the investment or the management of the portfolio of the securities or the funds of the client. “Portfolio” means the total holdings of securities belonging to any person.

A portfolio manager plays a pivotal role in deciding the best investment plan for an individual as per his income, age as well as ability to undertake risks. A portfolio manager is responsible for making an individual aware of the various investment tools available in the market and benefits associated with each plan. Make an individual realize why he actually needs to invest and which plan would be the best for him. A portfolio manager is responsible for designing customized investment solutions for the clients according to their financial needs.

SEBI (PORTFOLIO MANAGERS) REGULATIONS, 1993

SEBI issued SEBI (Portfolio Managers) Regulations, 1993 in exercise of the powers conferred by Section 30 of SEBI Act, 1992. These regulations took effect from 7th January, 1993.

Chapter I contains preliminary matters and definitions. Chapter II consisting Regulation 3 to 12 deal with the procedure for registration of portfolio managers.

Regulation 3 provides that a person shall not act as portfolio manager unless he holds a certificate granted by SEBI under these regulations. Regulation 3A lays down that an application by a portfolio manager for grant of the certificate shall be made to SEBI in the prescribed form-A and shall be accompanied by a non-refundable application fee, as specified in Clause (1) of Schedule II, to be paid in the manner specified in Part B thereof. Incomplete applications shall be rejected after the applicant is given an opportunity to remove within the time specified such objections on the application as may be indicated by SEBI. Before disposing the application, SEBI may require the applicant to furnish further information or clarification and the applicant or its principal officer who is mainly responsible for the activities as a portfolio manager, shall appear before SEBI to make a personal representation, if required.

NORMS FOR REGISTRATION AS PORTFOLIO MANAGERS

The requirements to be satisfied by the applicant for getting the certificate of registration as mentioned in Regulation 6 are as follows:

- (a) the applicant is a body corporate;
- (b) the applicant has the necessary infrastructure like adequate office space, equipment's and the manpower to effectively discharge the activities of a portfolio manager;
- (c) the principal officer of the applicant has either professional qualifications in finance, law, accountancy or business management from an institution recognised by the Government or a foreign university or an experience of at least 10 years in related activities in the securities market including in a portfolio manager, stock broker or as a fund manager and a CFA charter from the CFA Institute.
- (d) the applicant has in its employment minimum of two persons who, between them, have at least five years' experience as portfolio manager or stock broker or investment manager or in the areas related to fund management;
- (e) any previous application for grant of certificate made by any person directly or indirectly connected with the applicant has been rejected by SEBI;

- (f) any disciplinary action has been taken by SEBI against a person directly or indirectly connected with the applicant under the Act or the Rules or the Regulations made thereunder.
- (g) the applicant fulfils the capital adequacy requirements;
- (h) the applicant, its director, principal officer or the employee as specified in Clause (d) is involved in any litigation connected with the securities market which has an adverse bearing on the business of the applicant;
- (i) the applicant, its director, principal officer or the employee as specified in Clause (d) has at any time been convicted for any offence involving moral turpitude or has been found guilty of any economic offence;
- (j) the applicant is a fit and proper person;
- (k) grant of certificate to the applicant is in the interests of investors.

CAPITAL ADEQUACY REQUIREMENT

Regulation 7 lays down that portfolio manager must have capital adequacy requirement of not less than networth of two crore rupees. However the portfolio manager shall fulfill capital adequacy requirement under these regulations, separately and independently, of capital adequacy requirements if any for each activity undertaken by it under the relevant regulations. Networth for the purpose means the aggregate value of paid-up equity capital plus free reserves (excluding reserves created out of revaluation) reduced by the aggregate value of accumulated losses and deferred expenditure not written off, including miscellaneous expenses not written off.

SEBI on being satisfied that the applicant fulfils the requirement specified above shall send an intimation to the applicant. On payment of the requisite fees by the applicant in accordance with Clause 1A of Schedule II of the Regulations, he will be granted a certificate of Registration in Form-B.

CONDITIONS OF REGISTRATION

Any registration granted under these regulation shall be subject to the following conditions, namely:

- (a) where the portfolio manager proposes to change its status or constitution, it shall obtain prior approval of SEBI for continuing to act as such after the change;
- (b) it shall pay the fees for registration, in the manner provided in these regulations;
- (c) it shall take adequate steps for redressal of grievances of the investors within one month of the date of the receipt of the complaint and keep SEBI informed about the number, nature and other particulars of the complaints received;
- (d) it shall maintain capital adequacy requirements specified in these regulation at all times during the period of the certificate;
- (e) it shall abide by the regulations made under the Act in respect of the activities carried on by it as portfolio manager.

PERIOD OF VALIDITY OF CERTIFICATE

The certificate of registration granted under regulation 8 shall be valid unless it is suspended or cancelled by SEBI.

PROCEDURE WHERE REGISTRATION IS NOT GRANTED

Where the applicant does not satisfy the requirement of registration, SEBI may reject the application after giving an opportunity of being heard. The refusal shall be communicated by SEBI within 30 days of such refusal indicating the grounds for rejection. An applicant if aggrieved by SEBI's rejection may apply within a period of 30 days from the date of receipt of rejection letter to SEBI for reconsideration. SEBI shall reconsider the matter and communicate its final decision as soon as possible in writing to the applicant. The applicant shall cease to carry on activity as portfolio manager on receipt of rejection of his application. If the portfolio manager fails to pay the fees as provided in Schedule II, SEBI may suspend the certificate and during the period of suspension the portfolio manager shall not carry on activity as such portfolio manager.

CODE OF CONDUCT

Regulation 13 lays down that every portfolio manager shall abide by the code of conduct as specified in Schedule III to the Regulations.

CONTRACT WITH CLIENTS AND DISCLOSURES

Regulation 14 stipulates that the portfolio manager, before taking up an assignment of management of funds or portfolio of securities on behalf of a client, enter into an agreement in writing with such client clearly defining the *inter se* relationship and setting out their mutual rights, liabilities and obligations relating to the management of funds or portfolio of securities containing the details as specified in Schedule IV to the Regulations:

The agreement between the portfolio manager and the client shall, *inter alia*, contain:

- (i) the investment objectives and the services to be provided;
- (ii) areas of investment and restrictions, if any, imposed by the client with regard to the investment in a particular company or industry;
- (iii) type of instruments and proportion of exposure;
- (iv) tenure of portfolio investments;
- (v) terms for early withdrawal of funds or securities by the clients;
- (vi) attendant risks involved in the management of the portfolio;
- (vii) period of the contract and provision of early termination, if any;
- (viii) amount to be invested subject to the restrictions provided under these regulations;
- (ix) procedure of settling client's account including form of repayment on maturity or early termination of contract;
- (x) fees payable to the portfolio manager;
- (xi) the quantum and manner of fees payable by the client for each activity for which service is rendered by the portfolio manager directly or indirectly (where such service is outsourced);
- (xii) custody of securities;
- (xiii) in case of a discretionary portfolio manager a condition that the liability of a client shall not exceed his investment with the portfolio manager;
- (xiv) the terms of accounts and audit and furnishing of the reports to the clients as per the provisions of these regulations; and
- (xv) other terms of portfolio investment subject to these regulations.

The portfolio manager shall provide to the client, the Disclosure Document as specified in Schedule V, along with a certificate in Form C as specified in Schedule I, at least two days prior to entering into an agreement with the client.

The Disclosure Document, shall *inter alia* contain the following –

- (i) the quantum and manner of payment of fees payable by the client for each activity for which service is rendered by the portfolio manager directly or indirectly (where such service is outsourced);
- (ii) portfolio risks;
- (iii) complete disclosures in respect of transactions with related parties as per the accounting standards specified by the Institute of Chartered Accountants of India in this regard;
- (iv) the performance of the portfolio manager:

However, the performance of a discretionary portfolio manager shall be calculated using weighted average method taking each individual category of investments for the immediately preceding three years and in such cases performance indicators shall also be disclosed;

- (v) the audited financial statements of the portfolio manager for the immediately preceding three years.

The contents of the Disclosure Document would be certified by an independent chartered accountant.

The portfolio manager is required to file with SEBI, a copy of the Disclosure Document before it is circulated or issued to any person and every six months thereafter or whenever any material change is effected therein whichever is earlier, along with the certificate in Form C as specified in Schedule I. The portfolio manager shall ensure that the disclosure document is given to clients along with the account opening form atleast 2 days in advance of signing of the agreement.

The portfolio manager shall charge an agreed fee from the clients for rendering portfolio management services without guaranteeing or assuring, either directly or indirectly, any return and the fee so charged may be a fixed fee or a return based fee or a combination of both.

The portfolio manager may, subject to the disclosure in terms of the Disclosure Document and specific permission from the client, charge such fees from the client for each activity for which service is rendered by the portfolio manager directly or indirectly (where such service is outsourced).

RESPONSIBILITIES OF A PORTFOLIO MANAGER

Regulation 15 lays down that the discretionary portfolio manager shall individually and independently manage the funds of each client in accordance with the needs of a client in a manner which does not partake character of a mutual fund, whereas the non discretionary portfolio manager shall manage the funds in accordance with the directions of the client. The portfolio manager shall not accept from the client, funds or securities worth less than twenty five lacs rupees. The portfolio manager shall act in a fiduciary capacity with regard to the clients funds. The portfolio manager shall keep the funds of all clients in a separate account to be maintained by it in a Scheduled Commercial Bank. He shall transact in securities within the limitation placed by the client for dealing in securities under the provisions of RBI Act, 1934. He shall not derive any direct or indirect benefit out of the clients funds or securities. The portfolio manager shall not borrow funds or securities for behalf of the client. The portfolio manager shall not lend securities held on behalf of clients to a third person except as provided under these regulation.

INVESTMENT OF CLIENTS MONEY

Regulation 16 provides that the money or securities accepted by the portfolio manager shall not be invested or managed by the portfolio manager except in terms of the agreement between the portfolio manager and the client. Any renewal of portfolio fund on maturity of the initial period shall be deemed as a fresh placement. The funds or securities can be withdrawn or taken back by the client before the maturity of the contract under the following circumstances, namely –

- (a) voluntary or compulsory termination of portfolio management services by the portfolio manager or the client.
- (b) suspension or cancellation of the certificate of registration of the portfolio manager by SEBI.

(c) bankruptcy or liquidation of the portfolio manager.

The portfolio manager shall invest funds of his clients in money market instruments or derivatives or as specified in the contract:

However, leveraging of portfolio shall not be permitted in respect of investment in derivatives. Further, the portfolio manager shall not deploy the clients' funds in bill discounting, badla financing or for the purpose of lending or placement with corporate or non-corporate bodies. "Money market instruments" includes commercial paper, trade bill, treasury bills, certificate of deposit and usance bills.

The portfolio manager shall not while dealing with clients' funds indulge in speculative transactions that is, he shall not enter into any transaction for purchase or sale of any security which is periodically or ultimately settled otherwise than by actual delivery or transfer of security except the transactions in derivatives.

The portfolio manager shall, ordinarily purchase or sell securities separately for each client. However, in the event of aggregation of purchases or sales for economy of scale, *inter se* allocation shall be done on a *pro rata* basis and at weighted average price of the day's transactions. The portfolio manager shall not keep any open position in respect of allocation of sales or purchases effected in a day.

Any transaction of purchase or sale including that between the portfolio manager's own accounts and client's accounts or between two clients' accounts shall be at the prevailing market price.

The portfolio manager shall segregate each clients' funds and portfolio of securities and keep them separately from his own funds and securities and be responsible for safekeeping of clients' funds and securities.

The portfolio manager shall not hold the listed securities or unlisted securities, belonging to the portfolio account, in its own name on behalf of its clients either by virtue of contract with clients or otherwise. The portfolio managers, may, subject to authorization by the client in writing, participate in securities lending.

Foreign institutional investors and sub accounts registered with SEBI may avail of the services of a portfolio manager.

Every portfolio manager shall appoint a custodian in respect of securities managed or administered by it. However, this regulation shall not apply to a portfolio Manager who has total assets under management of value less than five hundred crore rupees; or who performs purely advisory functions.

ACCOUNTING BY PORTFOLIO MANAGERS

Regulations 17 to 20 deal with books of accounts, records, accounts and audit.

Regulation 17 lays down that every portfolio manager shall keep and maintain the following books of accounts, records and documents, namely - a) a copy each of balance sheet, profit and loss account and the auditor's account in respect of each accounting period b) a statement of financial position and c) records in support of every investment transaction or recommendation which will indicate the data, facts and opinions leading to that investment decision. Every portfolio manager shall intimate to SEBI where the books of accounts, records or documents are maintained. Every portfolio manager shall after the end of each accounting period furnish to SEBI copies of the balance sheet, profit and loss account and such other documents as are required under these regulations for any other preceeding five accounting years. Regulation 18 provides that portfolio manager shall furnish to SEBI half-yearly unaudited financial results when required by SEBI with a view to assist in monitoring the capital adequacy of the portfolio manager.

The portfolio manager shall preserve the books of account and other records and documents mentioned in any of the regulations mentioned under Chapter III for a minimum period of five years.

Regulation 20 lays down that the portfolio manager shall maintain separate client-wise accounts. The funds received from the clients, investments or disinvestments and all the credits to the account of the client like interest, dividend, bonus or any other beneficial interest received on the investment and debits for expenses if

any shall be properly accounted for and details thereof shall be reflected correctly in the clients accounts. The tax deducted at source as required under the Income Tax Act, 1961 shall be recorded in the portfolio account. The books of account will be audited by a qualified auditor to ensure that portfolio manager has followed proper accounting methods and procedures and that he has performed the duties in accordance with the law. A certificate to this effect shall, if so specified be submitted to SEBI within 6 months of the close of the portfolio managers accounting period.

The portfolio accounts of the portfolio manager shall be audited annually by an independent chartered accountant and a copy of the certificate issued by the chartered accountant shall be given to the client.

The client may appoint a chartered accountant to audit the books and accounts of the portfolio manager relating to his transactions and the portfolio manager shall co-operate with such chartered accountant in course of the audit.

REPORTS BY PORTFOLIO MANAGER TO THE CLIENT

Regulation 21 lays down that the portfolio manager shall furnish periodically a report to the client as agreed to in the contract but not exceeding a period of 6 months add as and when required by the client and such report shall contain the following details, namely –

- (a) the composition and the value of the portfolio, description of security, number of securities, value of each security held in a portfolio, cash balance and aggregate value of the portfolio as on the date of report.
- (b) transactions undertaken during the period of report including date of transaction and details of purchases and sales.
- (c) beneficial interest received during that period in respect of interest, dividend, bonus shares, rights shares and debentures.
- (d) expenses incurred in managing the portfolio of the client.
- (e) details of risk foreseen by the portfolio manager and the risk relating to the securities recommended by the portfolio manager for investment or disinvestment.

Regulation 21(1A) provides that the report may be made available on the website of the portfolio manager with restricted access to each client.

The portfolio manager shall in terms of the agreement with the client also furnish to the client documents and information relating only to the management of a portfolio. On termination of the contract, the portfolio manager shall give a detailed statement of accounts to the client and settle the account with the client as agreed in the contract. The client has the right to obtain details of his portfolio from the portfolio managers.

ACTION ON AUDITOR'S REPORT AND DISCLOSURE TO SEBI

Every portfolio manager shall within two months from the date of the auditor's report take steps to rectify the deficiencies made out in such report. A portfolio manager shall disclose to SEBI as and when required the information, namely - particulars regarding the management of a portfolio; any change in the information or particulars previously furnished which have a bearing on the certificate granted to him; the names of the clients whose portfolio he has managed; and particulars relating to the capital adequacy requirement.

COMPLIANCE OFFICER

Regulation 23A provides that every portfolio manager is required to appoint a compliance officer responsible for monitoring the compliance of the Act, rules and regulations, notifications, guidelines, instructions etc. issued by SEBI or the Central Government and for redressal of investors' grievances. The compliance officer should independently and immediately report to SEBI for any non-compliance observed by him.

INSPECTION AND DISCIPLINARY PROCEEDINGS

Regulations 24 to 29 contain provisions related to inspection and disciplinary proceeding by SEBI.

Regulation 24 empowers SEBI to appoint one or more persons as inspecting authority to under take the inspection of the books of accounts, records and documents of the portfolio manager to ensure that they are being maintained in the manner required, that the provisions of the Act, Rules and Regulations are being complied with. The inspecting authority shall investigate into the complaints received from the investors, other portfolio managers or any other person on any matter having a bearing on the activities of the portfolio manager and investigate *suo motu* in the interest of securities business or investors interest into the affairs of the portfolio manager.

SEBI shall give a reasonable notice to the portfolio manager before undertaking an inspection. However, where SEBI is satisfied that in the interest of the investors, no such notice should be given it may by an order in writing direct that the inspection of the affairs of the portfolio manager be taken up without such notice. During the course of the inspection the portfolio manager against whom an inspection is being carried out shall be bound to discharge his obligations as stated below:

OBLIGATIONS OF PORTFOLIO MANAGER

It shall be the duty of every director, proprietor, partner, officer and employee of the portfolio manager who is being inspected, to produce to the inspecting authority such books of accounts and documents in his custody or control and furnish him with the statements and information relating to these activities within such time as the inspecting authority may require. The portfolio manager shall allow the inspecting authority to have reasonable access to the premises occupied by the former or by any other person on his behalf and also extend reasonable facility for examining any books, records, documents and computer data in his possession or in the possession of any other person and also provide copies of documents or other material which in the opinion of the inspecting authority are relevant for the purposes of the inspection. In the course of inspection, the inspecting authority shall be entitled to examine or record statements of any principal officer, director, partner, proprietor and employee of the portfolio manager. It shall be the duty of each such person to give to the inspecting authority all assistance in connection with the inspection which the portfolio manager may reasonably be expected to give.

The inspecting authority shall submit an inspection report to SEBI as soon as it is possible. SEBI or the chairman shall after consideration of the inspection or investigation report take such action as SEBI or its chairman may deem fit and appropriate including action under Chapter V of SEBI (Intermediaries) Regulations, 2008.

LIABILITY FOR ACTION IN CASE OF DEFAULT

A portfolio manager who contravenes any of the provisions of the Act, Rules or Regulations framed there under shall be liable for one or more action specified therein including the action under Chapter V of SEBI (Intermediaries) Regulations, 2008.

APPOINTMENT OF AUDITOR

SEBI may appoint a qualified auditor to investigate into the books of account or the affairs of the portfolio manager.

The auditor so appointed shall have the same powers of the inspecting authority as are mentioned in regulation and the obligation of the portfolio manager and his employees in regulation 26 shall be applicable to the investigation under this regulation.

INTERNAL AUDIT OF PORTFOLIO MANAGER

Every Portfolio manager is required to appoint a Practising Company Secretary or a Practising Chartered Accountant for conducting the internal audit. The Portfolio manager is required to report the compliance of the aforesaid requirement to SEBI while submitting the half yearly report.

The report is to be submitted twice a year, as on 31st of March and 30th of September. The report should reach SEBI within thirty days of the period to which it relates.

No precise period has been prescribed for the PCS to submit his report to the Board of the company. However, it would be advisable for the PCS to give the audit report to the Portfolio Manager sufficiently well in advance to enable the Company to report the compliance of the same to SEBI.

The scope of the internal audit would comprise the checking of compliance of SEBI (Portfolio Managers) Regulations 1993 and circulars notifications or guidelines issued by SEBI and internal procedures followed by the Portfolio Manager.

ELIGIBLE FUND MANAGERS

The term “eligible fund manager” shall have the same meaning as assigned to it in sub section (4) of Section 9A of the Income-tax Act, 1961.

The term “eligible investment fund” shall have the same meaning as assigned to it in sub section (3) of Section 9A of the Income-tax Act, 1961.

Applicability

Regulation 12B of the SEBI (Portfolio Managers) Regulations, 1993 provides that the provisions of this regulations shall apply to eligible fund managers exclusively, pertaining to their activities as portfolio managers to eligible investment funds.

All other provisions of these regulations and the guidelines and circulars issued thereunder, unless the context otherwise requires or repugnant to the provisions of these regulations, shall apply to eligible fund managers in relation to their activities as portfolio managers to eligible investment funds.

Procedure to be followed by an existing Portfolio Manager

According to Regulation 12C stipulates that an existing portfolio manager may act as a portfolio manager to an eligible fund manager if:

- a) it fulfills all the conditions specified in sub section (4) of Section 9A of the Income-tax Act, 1961; and
- b) it intimates SEBI prior to undertaking such activity and submit declarations as specified in clause (1) of Schedule VI.

Procedure to be followed by an applicant for fresh registration

Regulation 12D provides that an applicant who is a company or a limited liability partnership or a body corporate who intends to act as an eligible fund manager may be granted registration if:

- a) it fulfills all the conditions specified in sub section (4) of Section 9A of the Income-tax Act, 1961;
- b) it complies with the requirements specified under Chapter II of these regulations, unless specified otherwise in this Chapter;
- c) it pays the fees as specified in Schedule II; and
- d) it provides a declaration to SEBI as specified in clause (2) of Schedule VI.

Obligation and Responsibilities of Eligible Fund Managers

Regulation 12E stipulates that an eligible fund manager shall be required to:

- 1) comply with the requirements specified under Section 9A of the Income-tax Act, 1961 or any amendment, notification, clarification, guideline issued thereon;

- 2) offer discretionary or non-discretionary or advisory services or a combination thereof to eligible investment funds;
- 3) operate in accordance to its mutually agreed contract with the eligible investment funds;
- 4) provide all material disclosures to eligible investment funds;
- 5) segregate funds and securities of each eligible investment fund;
- 6) segregate the funds and securities of eligible investment funds from that of its other clients;
- 7) maintain and segregate its books and accounts pertaining to its activities as a portfolio manager to eligible investment funds and other clients;
- 8) appoint a custodian; however, requirement of compliance to this sub-regulation does not arise in case an eligible investment fund has already appointed a custodian under the applicable act or regulations;
- 9) keep the funds of eligible investment funds in scheduled commercial banks; however, requirement of compliance to this sub-regulation does not arise in case an eligible investment fund does not intend to invest in Indian securities;
- 10) maintain any additional records as may be specified by SEBI and disclose the same to SEBI as and when required;
- 11) provide quarterly reports to SEBI;
- 12) ensure compliance with the Prevention of Money Laundering Act, 2002 and rules and regulations prescribed thereunder;
- 13) abide by the provisions in these regulations and circulars / guidelines issued from time to time by SEBI.

CUSTODIANS

A custodian is a person who carries on the business of providing custodial services to the client. The custodian keeps the custody of the securities of the client. The custodian also provides incidental services such as maintaining the accounts of securities of the client, collecting the benefits or rights accruing to the client in respect of securities.

Every custodian should have adequate facilities, sufficient capital and financial strength to manage the custodial services.

The SEBI (Custodian of Securities) Regulations, 1996 prescribe the roles and responsibilities of the custodians. According to the SEBI the roles and responsibilities of the custodians are to:

- Administrate and protect the assets of the clients.
- Open a separate custody account and deposit account in the name of each client.
- Record assets.
- Conduct registration of securities.

Custodial services refer to the safeguarding of securities of a client. The activities relating to custodial services involve collecting the rights benefiting the client in respect to securities, maintaining the securities' account of the client, informing the clients about the actions taken or to be taken, and maintaining records of the services.

The term "custodial services" in relation to securities of a client or gold or gold related instruments held by a mutual fund in accordance with the SEBI (Mutual Funds) Regulations, 1996 means safekeeping of securities or gold or gold related instruments or title deed of real estate assets and providing services incidental thereto, and includes –

- (i) maintaining accounts of securities or gold or gold related instruments or title deeds of real estate assets of a client;
- (ii) undertaking activities as a Domestic Depository in terms of the Companies (Issue of Indian Depository Receipts) Rules, 2004.
- (iii) collecting the benefits or rights accruing to the client in respect of securities or gold or gold related instruments or title deeds of real estate assets;
- (iv) keeping the client informed of the actions taken or to be taken by the issuer of securities, having a bearing on the benefits or rights accruing to the client; and
- (v) maintaining and reconciling records of the services referred to in points (i) to (iii).

SEBI (CUSTODIAN OF SECURITIES) REGULATIONS, 1996

In exercise of the powers conferred by section 30 of SEBI Act, 1992 SEBI notified the SEBI (Custodian of Securities) Regulations, 1996 on May 16, 1996.

Chapter I contains preliminary matter and definitions. Chapter II consisting Regulation 3 to 11 relating to procedure for registration of custodian

APPLICATION FOR GRANT OF CERTIFICATE

Regulation 3(1) provides that any person proposing to carry on business as custodian of securities on or after the commencement of these regulations shall make an application to SEBI for grant of a certificate. SEBI may, however in special cases, where it is of the opinion that it is necessary to do so for reasons to be recorded in writing, may extend the period upto a maximum of six months from the date of such commencement.

Any person who fails to make an application for grant of certificate within the period or the extended period specified therein, shall cease to carry on any activity as custodian of securities and shall be subject to the directions of SEBI with regard to the transfer of records, documents or securities relating to his activities as custodian of securities.

APPLICATION TO CONFORM TO REQUIREMENTS

An application which is not complete in all respects or which does not conform to the instructions specified therein will be rejected. However before rejecting any such application, SEBI would give the applicant an opportunity to remove the objection, within such time as may be specified.

FURNISHING OF INFORMATION

SEBI may require the applicant to furnish such further information or clarification regarding matters relevant to the activities of a custodian of securities for the purpose of consideration of the application. The applicant or his authorised representative may, if so required, appear before SEBI for personal representation, in connection with the grant of certificate.

CONSIDERATION OF APPLICATION FOR GRANT OF CERTIFICATE

SEBI, while granting the Certificate shall take into account following matters which are relevant to the activities of a custodian of securities:

- (a) the applicant fulfils the capital requirement;
- (b) the applicant has the necessary infrastructure, including adequate office space, vaults for safe custody of securities and computer systems capability, required to effectively discharge his activities as custodian of securities;

- (c) the applicant has the requisite approvals under any law for the time being in force, in connection with providing custodial services in respect of gold or gold related instruments of a mutual fund, or title deeds of real estate assets held by a real estate mutual funds scheme where applicable;
- (d) the applicant has in his employment adequate and competent persons who have the experience, capacity and ability of managing the business of the custodian of securities;
- (e) the applicant has prepared a complete manual, setting out the systems and procedures to be followed by him for the effective and efficient discharge of his functions and the arms length relationships to be maintained with the other businesses, if any, of the applicant;
- (f) the applicant is a person who has been refused a certificate by SEBI or whose certificate has been cancelled by SEBI;
- (g) the applicant, his director, his principal officer or any of his employees is involved in any litigation connected with the securities market;
- (h) the applicant, his director, his principal officer or any of his employees has at any time been convicted of any offence involving moral turpitude or of any economic offence;
- (i) the applicant is a fit and proper person; and
- (j) the grant of certificate is in the interest of investors.

Also SEBI shall not consider an application unless the applicant is a body corporate.

CAPITAL REQUIREMENT

Regulation 7(1) provides for the capital adequacy requirement. It provides that the applicant must have a net worth of a minimum of rupees fifty crores. The term “net worth” means the paid up capital and the free reserves as on the date of the application. Any applicant is permitted to fulfil his capital adequacy requirements within one month of the receipt of certificate.

PROCEDURE AND GRANT OF CERTIFICATE

Regulation 8(1) provides that after considering the application, if SEBI is satisfied that all particulars sought have been furnished and the applicant is eligible for the grant of a certificate, it will send an intimation of the same to the applicant.

On receipt of an intimation the applicant shall pay to SEBI specified registration fee. SEBI shall thereafter grant a certificate to the applicant on receipt of the registration fee. It has been provided that SEBI may restrict the certificate of registration to provide custodial services either in respect of securities or in respect of gold or gold related instruments of a client or title deeds of real estate assets held by a real estate mutual fund scheme.

A custodial of securities holding a certificate of registration may provide custodial services in respect of gold or gold related instruments of a mutual fund and in respect of title deeds of real estate assets held by a real estate mutual fund scheme, only after taking prior approval of the SEBI.

CONDITIONS OF CERTIFICATE

The certificate granted to the custodian of securities may be subject to the following conditions, namely:

- (a) it shall not commence any activities as custodian of securities unless it fulfils the capital requirement;
- (b) it shall abide by the provisions of the Act and these regulations in the discharge of its functions as custodian of securities;
- (c) it shall enter into a valid agreement with its client for the purpose of providing custodial services;

- (d) it shall pay annual fees as specified in these regulation;
- (e) if any information previously submitted by it to SEBI is found by it to be false or misleading in any material particular, or if there is any change in such information, it shall forthwith inform SEBI in writing; and
- (f) besides providing custodial services, it shall not carry on any activity other than activities relating to rendering of financial services.

PERIOD OF VALIDITY

Regulation 9A of the Regulations provide that every certificate granted under these regulation shall be valid for a period of three years from the date of grant.

RENEWAL OF CERTIFICATE

Regulation 9B provides that a custodian of securities, desirous of having its certificate renewed shall make an application to SEBI for renewal of the certificate in Form A, not less than three months before the expiry of its period of validity under Regulation 9A. The application for renewal of certificate shall be dealt with, as far as may be, as if it were an application for the grant of a fresh certificate and shall be accompanied with the application fee as specified in Schedule II.

PROCEDURE WHERE CERTIFICATE IS NOT GRANTED

Regulation 10(1) lays down that after considering an application for grant of certificate, if SEBI is satisfied that a certificate should not be granted, SEBI may reject the application after giving the applicant a reasonable opportunity of being heard.

The decision of SEBI rejecting the application shall be communicated within thirty days of such decision to the applicant in writing, stating therein the grounds on which the application has been rejected. An applicant, aggrieved by the decision of SEBI may within a period of thirty days from the date of receipt of communication apply to SEBI for re-consideration of its decision.

SEBI shall, as soon as possible, in the light of the submissions made in the application for re-consideration and after giving the applicant a reasonable opportunity of being heard, convey its decision in writing to the applicant.

EFFECT OF REFUSAL TO GRANT CERTIFICATE

Any custodian of securities whose application for grant of certificate has been rejected by SEBI shall, on and from the date of the receipt of the communication ceases to carry on any activity as custodian of securities and shall be subject to the directions of SEBI with regard to the transfer of records, documents or securities that may be in its custody or control relating to its activity as custodian of securities.

CODE OF CONDUCT

Every custodian of securities shall abide by the Code of Conduct as specified in the Third Schedule to the Regulations.

SEGREGATION OF ACTIVITIES

Regulation 13 provides that where a custodian of securities is carrying on any activity besides that of acting as custodian of securities, then the activities relating to his business as custodian of securities shall be separate and segregated from all other activities and its officers and employees engaged in providing custodial services shall not be engaged in any other activity carried on by him.

MECHANISM FOR MONITORING REVIEW

Regulation 14(1) provides that every custodian of securities shall have adequate mechanisms for the purposes

of reviewing, monitoring and evaluating the custodian's controls, systems, procedures and safeguards. The custodian of securities shall cause to be inspected annually the mechanism by an expert and forward the inspection report to SEBI within three months from the date of inspection.

PROHIBITION OF ASSIGNMENT

No custodian of securities shall assign or delegate its functions as a custodian of securities to any other person unless such person is a custodian of securities.

However, a custodian of securities may engage the services of a person not being a custodian, for the purpose of physical safekeeping of gold belonging to its client being a mutual fund having a gold exchange traded fund scheme, subject to the following conditions:

- (a) the custodian shall remain responsible in all respects to its client for safekeeping of the gold kept with such other person, including any associated risks;
- (b) all books, documents and other records relating to the gold so kept with the other person shall be maintained in the premises of the custodian or if they are not so maintained, they shall be made available therein, if so required by SEBI;
- (c) the custodian of securities shall continue to fulfill all duties to the clients relating to the gold so kept with the other person, except for its physical safekeeping."

SEPARATE CUSTODY ACCOUNT

Every custodian of securities is required to open a separate custody account for each client, in the name of the client whose securities are in its custody and ensure that the assets of one client would not be mixed with those of another client.

AGREEMENT WITH THE CLIENT

Every custodian of securities is required to enter into an agreement with each client on whose behalf it is acting as custodian of securities and every such agreement shall provide for the following matters, namely:

- (a) the circumstances under which the custodian of securities will accept or release securities, assets or documents from the custody account;
- (b) the circumstances under which the custodian of securities will accept or release monies from the custody account.
- (c) the circumstances under which the custodian of securities will receive rights or entitlements on the securities of the client;
- (d) the circumstances and the manner of registration of securities in respect of each client;
- (e) details of the insurance, if any, to be provided for by the custodian of securities.

INTERNAL CONTROLS

Every custodian of securities is required to have adequate internal controls to prevent any manipulation of records and documents, including audits for securities and rights or entitlements arising from the securities held by it on behalf of its client. Every custodian of securities would take appropriate safekeeping measures to ensure that such securities, assets or documents are protected from theft and natural hazard.

MAINTENANCE OF RECORDS AND DOCUMENTS

Regulation 19(1) provides that every custodian of securities is required to maintain the following records and documents, containing details of:

- (a) securities, assets or documents received and released on behalf of each client;
- (b) monies received and released on behalf of each client;
- (c) rights or entitlements of each client arising from the securities held on behalf of the client;
- (d) registration of securities in respect of each client;
- (e) ledger for each client;
- (f) instructions received from and sent to clients; and records of all reports submitted to SEBI.

The Custodian of securities would intimate to SEBI the place where the records and documents are maintained and custodian of securities shall preserve the records and documents maintained for a minimum period of five years.

The custodians shall submit the monthly reports latest by either the end of the third working day of the succeeding month or the 5th of the succeeding month, whichever is later. [SEBI Circular No. IMD/FPIC/CIR/P/2017/12 dated February 14, 2017]

APPOINTMENT OF COMPLIANCE OFFICER

Regulation 19A(1) provides that every custodian of securities would appoint a compliance officer responsible for monitoring the compliance of the Act, rules and regulations, notifications, guidelines, instructions etc. issued by SEBI or the Central Government. He is under an obligation for redressal of investors' grievances.

The compliance officer is required to immediately and independently report to SEBI any non-compliance observed by him.

INFORMATION TO SEBI

SEBI may, at any time, call for any information from a custodian of securities with respect to any matter relating to its activity as custodian of securities. Where any information is called for by SEBI, it shall be the duty of the custodian of securities to furnish such information, within such reasonable period as SEBI may specify.

INSPECTION AND AUDIT

SEBI may appoint one or more persons as inspecting officer to undertake inspection of the books of accounts, records and documents of the custodian of securities for any of the following purposes, namely:-

- (a) to ensure that the books of account, records and documents are being maintained by the custodian of securities in the manner specified in these regulations;
- (b) to investigate into complaints received from investors, clients or any other person, on any matter having a bearing on the activities of the custodian of securities;
- (c) to ascertain whether the provisions of the Act and these regulations are being complied with by the custodian of securities; and
- (d) to investigate *suo motu* into the affairs of the custodian of securities, in the interest of the securities market or in the interest of investors.

The custodian of securities against whom the inspection is being carried out is under an obligation to discharge his obligations.

OBLIGATIONS OF CUSTODIAN

It is the duty of the custodian of securities whose affairs are being inspected, and of every director, officer and employee thereof, to produce to the inspecting officer such books, securities, accounts, records and other documents in its custody or control and furnish him with such statements and information relating to his activities of the custodian of securities, as the inspecting officer may require, within such reasonable period as the inspecting officer may specify.

The custodian of securities is required to allow the inspecting officer to have reasonable access to the premises occupied by such custodian or by any other person on his behalf and also extend reasonable facility for examining any books, records, documents and computer data in the possession of the custodian of securities or such other person and also provide copies of documents or other materials which, in the opinion of the inspecting officer are relevant for the purposes of the inspection.

The inspecting officer, in the course of inspection, is entitled to examine or to record the statements of any director, officer or employee of the custodian of securities. It is the duty of every director, officer or employee of the custodian of securities to give to the inspecting officer all assistance in connection with the inspection, which the inspecting officer may reasonably require.

LIABILITY FOR ACTION IN CASE OF DEFAULT

A custodian of securities who contravenes any of the provisions of the Act, the rules framed thereunder or these regulations or fails to furnish any information relating to his activity as custodian of securities as required by SEBI or furnishes to SEBI information which is false and misleading in any material particular or does not submit periodic returns or reports as required by SEBI or does not co-operate in any enquiry or inspection conducted by SEBI or fails to update its systems and procedures as recommended by SEBI or fails to resolve the complaints of clients or fails to give a satisfactory reply to SEBI in this behalf or is guilty of misconduct or makes a breach of the Code of Conduct specified in the Third Schedule or fails to pay annual fees, shall be dealt with in the manner provided under Chapter V of SEBI (Intermediaries) Regulations, 2008.

INVESTMENT ADVISER

“Investment Adviser” means any person, who for consideration, is engaged in the business of providing investment advice to clients or other persons or group of persons and includes any person who holds out himself as an investment adviser, by whatever name called. Investment advisers are those, who guide one about his or her financial dealings and investments.

“Investment Adviser” means advice relating to investing in, purchasing, selling or otherwise dealing in securities or investment products, and advice on investment portfolio containing securities or investment products, whether written, oral or through any other means of communication for the benefits of the client and shall include financial planning. However, investment advice given through newspaper, magazines, any electronic or broadcasting or telecommunication medium, which is widely available to the public shall not be considered as investment advice for the purpose of these regulation.

The globalization of the capital markets, the proliferation of asset classes and the bewildering variety of risks that the average institutional investor is confronted which have increased the need for the specialized expertise that investment advisers provide. The role of investment adviser has got a lot of significance in the present time. Investment adviser serve as facilitators, making sure that all clients have many opportunities to express their financial concerns and issues. Basically Investment adviser give advice and provide services related to the investment management process. The rapid change of market conditions as well as the availability of numerous options for financial investments necessitates the existence of knowledgeable investment adviser. In order to add value, the investment adviser is called upon to apply specialized knowledge, experience and analytical resources to create and deliver focused advice to client and works to increase the investment

knowledge of clients and thereby support the fiduciary obligations clients face in the management of their plan.

SEBI (INVESTMENT ADVISERS) REGULATIONS, 2013

In exercise of the powers conferred by sub-section (1) of Section 30 read with clause (b) of sub-section (2) of Section 11 of SEBI Act, 1992, SEBI made these regulations.

REGISTRATION OF INVESTMENT ADVISERS

Regulation 3 deals with the application for grant of certificate by SEBI. A person shall not act as an investment adviser or hold itself out as an investment adviser unless he has obtained a certificate of registration from SEBI.

An application for grant of certificate of registration shall be made in Prescribed Form and shall be accompanied by a non refundable application fee to be paid in the manner specified in these regulations.

EXEMPTION FROM REGISTRATION

Regulation 4 provides that certain persons are exempted from the requirement of registration under regulation 3 subject to the fulfillment of the conditions stipulated therefor, –

- (a) Any person who gives general comments in good faith in regard to trends in the financial or securities market or the economic situation where such comments do not specify any particular securities or investment product;
- (b) Any insurance agent or insurance broker who offers investment advice solely in insurance products and is registered with Insurance Regulatory and Development Authority for such activity;
- (c) Any pension advisor who offers investment advice solely on pension products and is registered with Pension Fund Regulatory and Development Authority for such activity;
- (d) Any distributor of mutual funds, who is a member of a self regulatory organisation recognised by SEBI or is registered with an association of asset management companies of mutual funds, providing any investment advice to its clients incidental to its primary activity;
- (e) Any advocate, solicitor or law firm, who provides investment advice to their clients, incidental to their legal practise;
- (f) Any member of Institute of Chartered Accountants of India, Institute of Company Secretaries of India, Institute of Cost and Works Accountants of India, Actuarial Society of India or any other professional body as may be specified by SEBI, who provides investment advice to their clients, incidental to his professional service;
- (g) Any stock broker or sub-broker registered under SEBI (Stock Broker and Sub-Broker) Regulations, 1992, Portfolio Manager registered under SEBI (Portfolio Managers) Regulations, 1993 or merchant banker registered under SEBI (Merchant Bankers) Regulations, 1992, who provides any investment advice to its clients incidental to their primary activity:

However, such intermediaries shall comply with the general obligation(s) and responsibilities as specified in Chapter III of these regulations. Further the existing portfolio manager offering only investment advisory services may apply for registration under these regulations after expiry of his current certificate of registration as a portfolio manager;

- (h) Any fund manager, by whatever name called of a mutual fund, alternative investment fund or any other intermediary or entity registered with SEBI;

- (i) Any person who provides investment advice exclusively to clients based out of India. However, persons providing investment advice to Non-Resident Indian or Person of Indian Origin shall fall within the purview of these regulations;
- (j) Any representative and partner of an investment adviser which is registered under these regulations. However, such representative and partner shall comply with these regulations; and
- (k) Any other person as may be specified by SEBI.

QUALIFICATION & CERTIFICATION

- Investment Advisers are required to hold a professional qualification or post-graduate degree or post graduate diploma in finance, accountancy, business management, commerce, economics, capital market, banking, insurance or actuarial science from a university or an institution recognized by the Central Government or any State Government or a recognized foreign university or institution or association. Alternatively, advisers having a graduate in any discipline with experience of at least five years in activities relating to advice in financial products or securities or fund or asset or portfolio management are also qualified.
- Investment Advisers, their partners and their representatives should have a certification on financial planning or fund or asset or portfolio management or investment advisory services from NISM or from any other organization or institution including Financial Planning Standards Board (FPSB) India or stock exchange in India provided that such certification is accredited by NISM.
- Existing investment advisers and their representatives seeking registration under these regulations will have to obtain certification within two years from the date of commencement of these regulations. Investment advisers whose existing certificates which are due for expiry need to also obtain the above mentioned certification to continue their practice.

CAPITAL ADEQUACY

SEBI has also laid down capital adequacy requirements for corporate and individual distributors. Corporate distributors will require a minimum net worth of ₹ 25 lakh while individuals and partnership firms will require to possess tangible assets worth at least ₹ 1 lakh.

REGISTRATION

After complying with the investment advisers regulations, Investment advisers would need to register with SEBI by paying a non-refundable application fee of ₹ 5,000. Individual advisors will have to shell out a registration fee of ₹ 10,000 while corporate will have to cough up ₹1 lakh in addition to the application fee. This certificate will be valid for a period of five years.

GENERAL OBLIGATIONS AND RESPONSIBILITIES

Regulation 15 deals with the general obligation of Investment Advisers which are as follows :

- (1) An investment adviser shall act in a fiduciary capacity towards its clients and shall disclose all conflicts of interests as and when they arise.
- (2) An investment adviser shall not receive any consideration by way of remuneration or compensation or in any other form from any person other than the client being advised, in respect of the underlying products or securities for which advice is provided.
- (3) An investment adviser shall maintain an arms-length relationship between its activities as an investment adviser and other activities.

- (4) An investment adviser which is also engaged in activities other than investment advisory services shall ensure that its investment advisory services are clearly segregated from all its other activities.
- (5) An investment adviser shall ensure that in case of any conflict of interest of the investment advisory activities with other activities, such conflict of interest shall be disclosed to the client.
- (6) An investment adviser shall not divulge any confidential information about its client, which has come to its knowledge, without taking prior permission of its clients, except where such disclosures are required to be made in compliance with any law for the time being in force.
- (7) An investment advisor shall not enter into transactions on its own account which is contrary to its advice given to clients for a period of fifteen days from the day of such advice.

However, during the period of such fifteen days, if the investment adviser is of the opinion that the situation has changed, then it may enter into such a transaction on its own account after giving such revised assessment to the client at least 24 hours in advance of entering into such transaction.

- (8) An investment adviser shall follow Know Your Client procedure as specified by SEBI from time to time.
- (9) An investment adviser shall abide by Code of Conduct as specified in Third Schedule.
- (10) An investment adviser shall not act on its own account, knowingly to sell securities or investment products to or purchase securities or investment product from a client.
- (11) In case of change in control of the investment adviser, prior approval from SEBI shall be taken.
- (12) Investment advisers shall furnish to SEBI information and reports as may be specified by SEBI from time to time.
- (13) It shall be the responsibility of the Investment Adviser to ensure that its representatives and partners, as applicable, comply with the certification and qualification requirements under these Regulation at all times.

MAINTENANCE OF RECORDS

Regulation 19 provides that an investment adviser shall maintain the following records,-

- (a) Know Your Client records of the client;
- (b) Risk profiling and risk assessment of the client;
- (c) Suitability assessment of the advice being provided;
- (d) Copies of agreements with clients, if any;
- (e) Investment advice provided, whether written or oral;
- (f) Rationale for arriving at investment advice, duly signed and dated;
- (g) A register or record containing list of the clients, the date of advice, nature of the advice, the products/ securities in which advice was rendered and fee, if any charged for such advice.

All records shall be maintained either in physical or electronic form and preserved for a minimum period of five years. However, where records are required to be duly signed and are maintained in electronic form, such records shall be digitally signed.

LIABILITY FOR ACTION IN CASE OF DEFAULT

Regulation 28 provides that an investment adviser who –

- (a) contravenes any of the provisions of the Act or any regulations or circulars issued thereunder;
- (b) fails to furnish any information relating to its activity as an investment adviser as required by SEBI;
- (c) furnishes to SEBI information which is false or misleading in any material particular;
- (d) does not submit periodic returns or reports as required by SEBI;
- (e) does not co-operate in any enquiry, inspection or investigation conducted by the SEBI;
- (f) fails to resolve the complaints of investors or fails to give a satisfactory reply to SEBI in this behalf,

shall be dealt within the manner provided under the SEBI (Intermediaries) Regulations, 2008

AUDIT OF INVESTMENT ADVISER

According to Regulation 19(3) an investment adviser shall conduct yearly audit in respect of compliance with these regulations from a member of Institute of Chartered Accountants of India or Institute of Company Secretaries of India.

PART B

GUIDELINES ON ANTI MONEY LAUNDERING MEASURES

The Prevention of Money Laundering Act, 2002 (PMLA) has been brought into force with effect from 1st July 2005. Necessary Notifications / Rules under the said Act have been published in the Gazette of India on 1st July 2005 by the Department of Revenue, Ministry of Finance, Government of India. SEBI has laid down obligations of securities market intermediaries under PMLA, 2002 and rules framed thereunder.

As per the provisions of PML the Act, every banking company, financial institution (which includes chit fund company, a co-operative bank, a housing finance institution and a non-banking financial company) and intermediary (which includes a stock-broker, sub-broker, share transfer agent, banker to an issue, trustee to a trust deed, registrar to an issue, merchant banker, underwriter, portfolio manager, investment adviser and any other intermediary associated with securities market and registered under section 12 of the Securities and Exchange Board of India Act, 1992) shall have to maintain a record of all the transactions; the nature and value of which has been prescribed in the Rules notified under the PMLA. Such transactions include:

- All cash transactions of the value of more than Rs 10 lakhs or its equivalent in foreign currency.
- All series of cash transactions integrally connected to each other which have been valued below Rs 10 lakhs or its equivalent in foreign currency where such series of transactions take place within one calendar month.
- All suspicious transactions whether or not made in cash and including *inter alia*, credits or debits into from any non-monetary account such as demat account, security account maintained by the registered intermediary.

It may, however, be clarified that for the purpose of suspicious transactions, reporting apart from 'transactions integrally connected', 'transactions remotely connected or related should also be considered.

SEBI has laid down the minimum requirements / disclosures to be made in respect of clients. The intermediaries are required to specify additional disclosures to be made by clients to address concerns of Money Laundering and suspicious transactions undertaken by clients, according to their requirements.

The intermediaries are also required to designate an officer as 'Principal Officer' who would be responsible for ensuring compliance of the provisions of the PMLA and also designate a person as a 'Designated Director' on whom the director, FIU-IND can take appropriate action including levying monetary penalty on the designated director for failure of the intermediary to comply with any of its AML/CFT obligation.

Each registered intermediary should adopt written procedures to implement the anti money laundering provisions as envisaged under the Anti Money Laundering Act, 2002. Such procedures should include *inter alia*, the following three specific parameters which are related to the overall 'Client Due Diligence Process':

- (a) Policy for acceptance of clients
- (b) Procedure for identifying the clients
- (c) Transaction monitoring and reporting especially Suspicious Transactions Reporting (STR)

OBLIGATIONS OF INTERMEDIARIES UNDER PREVENTION OF MONEY LAUNDERING ACT, 2002

Section 12 of the Prevention of Money Laundering Act, 2002 lays down following obligations on an intermediary:

Every banking company, financial institution and intermediary shall –

- (A) maintain a record of all transactions, the nature and value of which may be prescribed, whether such transactions comprise of a single transaction or a series of transactions integrally connected to each other, and where such series of transactions take place within a month;
- (B) furnish information of transactions referred to in clause (a) to the Director within such time as may be prescribed;
- (C) verify and maintain the records of the identity of all its clients, in such a manner as may be prescribed.

However, where the principal officer of an Intermediary or financial institution or intermediary, as the case may has reason to believe that a single transaction or series of transactions integrally connected to each other have been valued below the prescribed limit so as to defeat the provisions of this section, such officer shall furnish information in respect of such transactions to the Director within the prescribed time.

The records shall be maintained for a period of ten years from the date of cessation of the transactions between the clients of the banking company or financial institution or intermediary, as the case may be.

CASH TRANSACTION REPORT

The Prevention of Money Laundering Act, 2002 and the Rules thereunder require every intermediary to furnish details of the following cash transactions:

- (A) All cash transactions of the value of more than rupees ten lakhs or its equivalent in foreign currency.
- (B) All series of cash transactions integrally connected to each other which have been valued below rupees ten lakhs or its equivalent in foreign currency where such series of transactions have taken place within a month.

SUSPICIOUS TRANSACTION REPORT

The Prevention of Money Laundering Act, 2002 and the Rules notified thereunder require every intermediary to furnish details of suspicious transactions whether or not made in cash. Suspicious transaction means a transaction whether or not made in cash which, to a person acting in good faith –

- (a) gives rise to a reasonable ground of suspicion that it may involve the proceeds of crime; or
- (b) appears to be made in circumstances of unusual or unjustified complexity; or
- (c) appears to have no economic rationale or bonafide purpose.

Broad categories of reason for suspicion and examples of suspicious transactions for an intermediary are indicated as under:

Identity of Client

- False identification documents
- Identification documents which could not be verified within reasonable time
- Non-face to face client
- Doubt over the real beneficiary of the account
- Accounts opened with names very close to other established business entities

Suspicious Background

- Suspicious background or links with known criminals

Multiple Accounts

- Large number of accounts having a common account holder, introducer or authorized signatory with no rationale
- Unexplained transfers between multiple accounts with no rationale

Activity in Accounts

- Unusual activity compared to past transactions
- Use of different accounts by client alternatively
- Sudden activity in dormant accounts
- Activity inconsistent with what would be expected from declared business
- Account used for circular trading

Nature of Transactions

- Unusual or unjustified complexity
- No economic rationale or bonafide purpose
- Source of funds are doubtful
- Appears to be case of insider trading
- Investment proceeds transferred to a third party
- Transactions reflect likely market manipulations
- Suspicious off market transactions

Value of Transactions

- Value just under the reporting threshold amount in an apparent attempt to avoid reporting
- Large sums being transferred from overseas for making payments
- Inconsistent with the clients apparent financial standing

- Inconsistency in the payment pattern by client
- Block deal which is not at market price or prices appear to be artificially inflated/deflated

CLIENT IDENTIFICATION PROCEDURE

The 'Know your Client' (KYC) policy should clearly spell out the client identification procedure to be carried out at different stages i.e. while establishing the intermediary – client relationship, while carrying out transactions for the client or when the intermediary has doubts regarding the veracity or the adequacy of previously obtained client identification data. SEBI has prescribed the minimum requirements relating to KYC for certain class of the registered intermediaries from time to time. Taking into account the basic principles enshrined in the KYC norms which have already been prescribed or which may be prescribed by SEBI from time to time, all registered intermediaries should frame their own internal guidelines based on their experience in dealing with their clients and legal requirements as per the established practices. Further, the intermediary should also maintain continuous familiarity and follow-up where it notices inconsistencies in the information provided. The underlying principle should be to follow the principles enshrined in the PML Act, 2002 as well as the SEBI Act, 1992 so that the intermediary is aware of the clients on whose behalf it is dealing.

INFORMATION TO BE MAINTAINED

Intermediaries are required to maintain and preserve the following information in respect of transactions mentioned above.

- (i) the nature of the transactions;
- (ii) the amount of the transaction and the currency in which it was denominated;
- (iii) the date on which the transaction was conducted; and
- (iv) the parties to the transaction.

MAINTENANCE AND PRESERVATION OF RECORDS

Intermediaries are required to take appropriate steps to evolve an internal mechanism for proper maintenance and preservation of such records and information in a manner that allows easy and quick retrieval of data as and when requested by the competent authorities. Further, the records have to be maintained and preserved for a period of ten years from the date of cessation of the transactions between the client and intermediary.

Records evidencing the identity of its clients and beneficial owners as well account files and business correspondence shall be maintained and preserved for a period of five years after the business relationship between a client and intermediary has ended or the account has been closed, whichever is later.

REPORTING TO FINANCIAL INTELLIGENCE UNIT-INDIA

In terms of the PMLA rules, intermediaries are required to report information relating to cash and suspicious transactions to the Director, Financial Intelligence Unit-India (FIU-IND) at the following address:

Director, FIU-IND,
Financial Intelligence Unit-India,
6th Floor, Hotel Samrat, Koutilya Marg,
Chanakyapuri, New Delhi-110021.
Website: <http://fiuindia.gov.in>

The Intermediaries are required to adhere to the following:

- (a) The cash transaction report (CTR) (wherever applicable) for each month should be submitted to FIU-IND by 15th of the succeeding month.
- (b) The Suspicious Transaction Report (STR) should be submitted within 7 days of arriving at a conclusion

that any transaction, whether cash or non-cash, or a series of transactions integrally connected are of suspicious nature. The Principal Officer should record his reasons for treating any transaction or a series of transactions as suspicious. It should be ensured that there is no undue delay in arriving at such a conclusion.

- (c) The Principal Officer is responsible for timely submission of CTR and STR to FIU-IND;
- (d) Utmost confidentiality is to be maintained in filing of CTR and STR to FIU-IND. The reports may be transmitted by speed/registered post/fax at the notified address.

The Trading Member should not put any restrictions on operations in the accounts where an STR has been made. Further, it should be ensured that there is no tipping off to the client at any level.

It is clarified that the registered intermediaries, irrespective of the amount of transaction and/or the threshold limit envisaged for predicate offences specified in Part B of Schedule of PMLA, 2002, should file STR if they have reasonable grounds to believe that the transactions involve proceeds of crime.

SEBI (INTERMEDIARIES) REGULATIONS, 2008

In the present regime a dozen regulations govern different categories of intermediaries. The broad framework of such regulations is similar to one another. SEBI in exercise of the powers conferred by section 30 of the Securities and Exchange Board of India Act, 1992 issued the SEBI (Intermediaries) Regulations, 2008 which seek to consolidate the common requirements and put in place a comprehensive framework which will apply to the intermediaries and prescribe the obligations, procedure, limitations etc. in so far as the common requirements are concerned. The new regulations seek to simplify procedures to make the registration/ regulation process of intermediaries less burdensome and cost effective without diluting the regulatory oversight. The regulation is primarily principle based and some significant changes in the framework are given below :

1. Permanent Registration

Subject to compliance with the SEBI Act, regulations, updation of relevant disclosures and payment of fees registration shall be permanent.

2. Registration for multiple activities

The process for registration for undertaking multiple activities by the same intermediary has been simplified.

3. Registration Form- information divided into two parts

Part 1 of the form will be disclosed and available to the public and Part II will contain such information which will be retained with SEBI as regulatory filing.

4. Fit and Proper person requirements

The criteria to determine whether the intermediary is a Fit and Proper person have been revised and are now principle based.

5. Suspension/Cancellation of certificate of registration

The manner of suspension/cancellation of any certificate granted to any person has been provided in the regulations. Consequently, the SEBI (Procedure for holding enquiry by enquiry officer and imposing penalty) Regulations, 2002 has been repealed and SEBI (Intermediaries) Regulations, 2008 has taken place.

APPLICATION FOR GRANT OF CERTIFICATE

(1) Regulation 3 provides that an application for grant of a certificate to act as an intermediary, shall be made to the SEBI in Form A of Schedule I with such additional information as required and the application fee, as specified.

However, the applicant seeking registration to act as a stock broker or sub-broker or a trading member or a clearing member or a depository participant shall make the application along with such additional information

through the stock exchange or through the clearing corporation of which the applicant is a member or trading member or through the depository in which the applicant proposes to act as a participant, as the case may be.

(2) The stock exchange, the clearing corporation, the depository or the specified self regulatory organization, as the case may be, shall examine the eligibility of the applicant in terms of these regulations, relevant regulations and the rules, regulations or bye-laws of the concerned stock exchange, clearing corporation, depository or the self regulatory organization and forward the application with the application fees to SEBI along with its recommendation as early as possible but not later than thirty days of receipt of the complete application with the specified application fees.

(3) An intermediary, who was granted a certificate under the relevant regulations prior to the commencement of these regulations in relation to such intermediary, may continue to act as such, subject to the following –

- (a) where the certificate was granted for a specified period, an application for grant of certificate under sub-regulation (1) shall be made by the intermediary at least three months prior to the expiry of such period or three months prior to expiry of two years from the commencement of these regulations in relation to such intermediary, whichever is earlier and if the intermediary fails to do so, it shall cease to act as an intermediary on and from the expiry of the aforementioned period;
- (b) where a certificate has been granted to an intermediary on a permanent basis, the certificate may continue to be valid under these regulations subject to the condition that the intermediary shall, within two years of commencement of these regulations in relation to such intermediary, furnish the information in Form A to SEBI and upload the information in Part I thereof on the website specified by SEBI:

However, the time may be extended by SEBI up to a period of six months on sufficient reasons being shown by the intermediary.

(4) An intermediary who has complied with the provisions of these regulations shall be deemed to have been granted certificate under these regulations, subject to the payment of fees specified under the relevant regulations.

(5) An applicant or an intermediary as the case may be, may carry on the activities of one or more intermediaries only if it obtains a separate certificate to carry on each such activity.

DISCLOSURE OF INFORMATION

Regulation 4 stipulates that the information contained in Part I of Form A shall be disclosed to the public by uploading such information on the website as specified by SEBI.

However, the other relevant information furnished by the intermediary in Part II of Form A which relates to commercial confidence and private information of the intermediary, may be treated as confidential by SEBI.

Any material change in the information furnished or uploaded under these regulations shall be updated by the intermediary promptly but not later than fifteen days of the occurrence of such change.

FURNISHING OF INFORMATION AND CLARIFICATION

Regulation 5 lays down that SEBI may require the applicant to furnish further information or clarifications, regarding matters relevant to the activity of such an intermediary and the applicant shall furnish such information and clarification to the satisfaction of SEBI, within the time specified.

VERIFICATION OF INFORMATION

Regulation 6 deals with the verification part. While considering the application, SEBI may, if it so desires, verify the information by physical verification of documents, office space, and inspect the availability of office space, infrastructure, and technological support which the applicant is required to have. For the purpose under sub-regulation (1), SEBI may appoint any person including an auditor.

CONSIDERATION OF APPLICATION

As per regulation 7 while considering an applicant, SEBI shall take into account all matters which it deems relevant to the activities in the securities market, including but not limited to the following—

- (a) whether the applicant or any of its associates have in the past been refused certificate by SEBI and if so, the ground for such refusal;
- (b) whether the applicant, its directors or partners, or trustees, as the case may be or its principal officer is involved in any pending litigation connected with the securities market which has an adverse bearing on the business of the applicant or on development or functioning of the securities markets;
- (c) whether the applicant satisfies the eligibility criteria and other requirements;
- (d) whether the grant of a certificate to the applicant is in the interest of the investors and the development of the securities market.

Any application for grant of certificate:

- (a) which is not complete in all respects and does not conform to the requirements in Form A and the requirements specified in the relevant regulation;
- (b) which does not contain such additional information as required;
- (c) which is incorrect, false or misleading in nature;
- (d) where the applicant is not in compliance with the eligibility requirements;
- (e) where the applicant is not a 'fit and proper person' as stated in Schedule II;
- (f) where the principal officer does not have the requisite qualification or experience as required under the relevant regulations;

shall be rejected by SEBI for reasons to be recorded by SEBI in writing. Before rejecting an application, the applicant shall be given an opportunity in writing to make good the deficiencies within the time specified by SEBI, for the purpose. Where an application is rejected for the reason that it contains false or misleading information, no such opportunity may be given and the applicant shall not make any application for grant of certificate under these regulations or any other regulations for a period of one year from the date of such rejection.

PROCEDURE FOR GRANT OF CERTIFICATE

Regulation 8 stipulates that SEBI on being satisfied that the applicant is eligible, shall grant a certificate in the form specified in the relevant regulations and send an intimation to the applicant in this regard:

However, where a pending proceeding before SEBI or any court or tribunal may result in the suspension or cancellation of the certificate, SEBI may give a conditional registration.

When an intermediary, who has been granted a certificate and who has filed Form A under these regulations, wishes to commence a new activity which requires a separate certificate under the relevant regulations, it shall, while seeking such certificate, not be required to file Form A, and shall furnish to SEBI only such additional information as is required under the relevant regulations.

CONDITIONS OF CERTIFICATE

Regulation 9 provides that any certificate granted by SEBI to an intermediary shall be subject to the following conditions, namely : –

- (a) where the intermediary proposes to change its status or constitution, it shall obtain prior approval of

SEBI for continuing to act as an intermediary after such change in status or constitution. A request in this regard shall be disposed off by SEBI within a period of sixty days from the date of receipt of such request and where the decision of SEBI has not been communicated to the intermediary within the said period of sixty days, the prior approval shall be deemed to have been granted and it shall contain the information in Form A;

- (b) it shall pay the applicable fees in accordance with the relevant regulations;
- (c) it shall abide by the provisions of the securities laws and the directions, guidelines and circulars as may be issued thereunder;
- (d) it shall continuously comply with the requirements of disclosure norms;
- (e) it shall meet the eligibility criteria and other requirements specified.

However, SEBI may impose other conditions as it may deem fit.

EFFECT OF REFUSAL TO GRANT CERTIFICATE OR EXPIRY OF CERTIFICATE

Regulation 10 provides that where an intermediary has failed to make an application or where an existing intermediary has been refused grant of certificate under these regulations, the intermediary shall:

- (a) forthwith cease to act as such intermediary;
- (b) transfer its activities to another intermediary which has been granted a certificate for carrying on such activity and allow its clients or investors to withdraw or transfer their securities or funds held in its custody without any additional cost to such client or investor;
- (c) make provisions as regards liability incurred or assumed by the intermediary;
- (d) take such other action, within the time period and in the manner, as may be required.

While refusing grant of certificate under these regulations to an intermediary, SEBI may impose such conditions upon the intermediary as it deems fit for protection of investors or clients of the intermediary or the securities market and such conditions shall be complied with.

PERIOD OF VALIDITY OF CERTIFICATE

The certificate granted to an intermediary shall be permanent unless surrendered by the intermediary or suspended or cancelled in accordance with these regulations.

GENERAL OBLIGATIONS

Regulation 12 lays down the general obligation of the intermediary. An intermediary shall provide SEBI with a certificate of its compliance officer on the 1st April of each year certifying;

- (a) the compliance by the intermediary on a continuous basis under these regulations and the relevant regulations;
- (b) disclosures made in Form A true and complete.

Each intermediary shall prominently display a photocopy of the certificate at all its offices including branch offices and also the name and contact details of the compliance officer to whom complaint may be made in the event of any investor grievance.

REDRESSAL OF INVESTOR GRIEVANCES

Regulation 13 provides that the intermediary shall make endeavours to redress investor grievances promptly but not later than forty-five days of receipt thereof and when called upon by SEBI to do so it shall redress the grievances of investors within the time specified by SEBI.

The intermediary shall at the end of each quarter of a Financial Year ending on 31st March upload information about the number of investor grievances received, redressed and those remaining unresolved beyond three months of the receipt thereof by the intermediary on the website specified by SEBI.

APPOINTMENT OF COMPLIANCE OFFICER

Regulation 14 of these regulations provides that an intermediary shall appoint a compliance officer for monitoring the compliance by it of the requirements where applicable. The intermediary may not appoint compliance officer if it is not carrying on the activity of the intermediary.

The compliance officer shall report to the intermediary or its board of directors, in writing, of any material non-compliance by the intermediary.

INVESTMENT ADVICE

Regulation 15 provides that an intermediary, its directors, officers, employees or key management personnel shall not render, directly or indirectly, any investment advice about any security in the publicly accessible media, whether real-time or non-real-time, unless a disclosure of its interest, direct or indirect, including its long or short position in the said security has been made, while rendering such advice and also discloses the interest of his dependent family members and that of the employer including employer's long or short position in the said security.

An intermediary shall not make a recommendation to any client or investor who may be expected to rely thereon to acquire, dispose of or retain any securities unless he has reasonable grounds to believe that the recommendation is suitable.

CODE OF CONDUCT

Regulation 16 stipulates that an intermediary and its directors, officers, employees and key management personnel shall continuously abide by the code of conduct specified in Schedule III.

INSPECTION OF BOOKS, ACCOUNTS AND RECORDS

The intermediary shall maintain such books, accounts and records as specified in the relevant regulations. Regulation 17 provides that without prejudice to the provisions of section 11 and section 11C of the Act, SEBI may appoint one or more persons as inspecting authority to undertake the inspection of the books, accounts, records including telephone records and electronic records and documents of an intermediary for any purpose.

The purposes may include:

- (a) to ensure that the books of account, records including telephone records and electronic records and documents are being maintained in the manner required under the relevant regulations;
- (b) to ascertain whether adequate internal control systems, procedures and safeguards have been established and are being followed by the intermediary to fulfill its obligations under the relevant regulations;
- (c) to ascertain whether any circumstances exist which would render the intermediary unfit or ineligible;
- (d) to ascertain whether the provisions of the securities laws and the directions or circulars issued thereunder are being complied with;
- (e) to inquire into the complaints received from investors, clients, other market participants or any other person on any matter having a bearing on the activities of the intermediary;
- (f) to inquire *suo motu* into such matters as may be deemed fit in the interest of investors or the securities market.

NOTICE BEFORE INSPECTION

Regulation 18 stipulates that before undertaking an inspection, the inspecting authority shall give a notice to the concerned intermediary. If the inspecting authority is satisfied that in the interest of the investors no such notice should be given, it may, for reasons to be recorded in writing, dispense with such notice.

OBLIGATIONS OF INTERMEDIARY ON INSPECTION

Regulation 19 provides that –

- (1) It shall be the duty of every director, proprietor, partner, trustee, officer, employee and any agent of an intermediary which is being inspected, to produce to the inspecting authority such books, accounts, records including telephone records and electronic records and documents in his custody or control and furnish to the inspecting authority with such statements and information relating to its activities within such time as the inspecting authority may require.
- (2) The intermediary shall allow the inspecting authority to have reasonable access to the premises occupied by such intermediary or by any other person on its behalf and also extend reasonable facility for examining such documents.
- (3) The inspecting authority shall, in the course of inspection, be entitled to examine or record statements of any principal officer, director, trustee, partner, proprietor or employee of such intermediary.
- (4) It shall be the duty of every director, proprietor, trustee, partner, officer and employee of such intermediary to give to the inspecting authority all assistance which the inspecting authority may reasonably require in connection with the inspection.

APPOINTMENT OF AUDITOR OR VALUER

Regulation 20 provides that SEBI may appoint a qualified auditor to inspect the books of account or the affairs of an intermediary. The auditor so appointed shall have the same powers of the inspecting authority.

SUBMISSION OF REPORT TO SEBI

As per regulation 21, the inspecting authority shall submit an inspection report including interim reports to SEBI. On submission of the inspection report, SEBI may take such action thereon as it may deem fit and appropriate.

CANCELLATION OR SUSPENSION OF REGISTRATION AND OTHER ACTIONS

Regulation 23 provides that where any person who has been granted a certificate of registration under the Act or regulations made thereunder –

- (a) fails to comply with any conditions subject to which a certificate of registration has been granted to him;
- (b) contravenes any of the provisions of the securities laws or directions, instructions or circulars issued thereunder.

SEBI may, without prejudice to any action under the securities laws or directions, instructions or circulars issued thereunder, by order take such action in the manner provided under these regulations.

APPOINTMENT OF DESIGNATED AUTHORITY

Regulation 24 provides that where it appears to the designated member, that any person who has been granted certificate of registration under the Act, regulations made thereunder has committed any default of the nature specified in regulation 23, he may appoint an officer not below the rank of a Division Chief, as a designated authority.

However, the designated member may, at his discretion, appoint a bench of three officers, each of whom shall not be below the rank of a Division Chief and such bench shall be presided by the senior most amongst them and all the decisions or recommendations of such bench shall be by way of majority.

No officer who has conducted investigation or inspection in respect of the alleged violation shall be appointed as a designated authority.

ISSUANCE OF NOTICE

As per regulation 25, the designated authority shall, if it finds reasonable grounds to do so, issue a notice to the

concerned person requiring him to show cause as to why the certificate of registration granted to it, should not be suspended or cancelled or why any other action provided herein should not be taken.

Every notice shall specify the contravention alleged to have been committed by the noticee copies of documents containing the findings arrived at in an investigation or inspection, if any, carried out.

The noticee shall be called upon to submit within a period to be specified in the notice, not exceeding twenty-one days from the date of service thereof, a written representation along with documentary evidence, if any, in support of the representation to the designated authority.

REPLY BY THE NOTICEE

Regulation 26 provides that the noticee shall submit to the designated authority its written representation within the period specified in the notice along with documentary evidence, if any, in support thereof. The designated authority may extend the time specified in the notice for sufficient grounds shown by the noticee and after recording reasons in writing.

EX-PARTE PROCEEDINGS

The noticee does not reply to the show cause notice, the designated authority may proceed with the matter ex-parte recording the reasons for doing so and make recommendation as the case may be on the basis of material facts available before it.

ACTION IN CASE OF DEFAULT

Regulation 27 provides for the following in case of default –

- (i) suspension of certificate of registration for a specified period;
- (ii) cancellation of certificate of registration;
- (iii) prohibiting the noticee to take up any new assignment or contract or launch a new scheme for the period specified in the order;
- (iv) debarring a principal officer of the noticee from being employed or associated with any registered intermediary or other registered person for the period specified in the order;
- (v) debarring a branch or an office of the noticee from carrying out activities for the specified period;
- (vi) warning the noticee.

PROCEDURE FOR ACTION ON RECEIPT OF THE RECOMMENDATION

Regulation 28 provides that on receipt of the report recommending the measures from the designated authority, the designated member shall consider the same and issue a show cause notice to the noticee enclosing a copy of the report submitted by the designated authority calling upon the noticee to submit its written representation as to why the action, including passing of appropriate direction, as the designated member considers appropriate, should not be taken.

The noticee may, within twenty one days of receipt of the notice send a reply to the designated member who may pass appropriate order after considering the reply, if any received from the noticee and providing the person with an opportunity of being heard, as expeditiously as possible and endeavour shall be made to pass the order within one hundred and twenty days from the date of receipt of reply of the notice or hearing.

INTIMATION OF THE ORDER

As per Regulation 29 and 30 deals with the order pass by the designated member. The designated member may pass a common order in respect of a number of notices where the subject matter in question is substantially the same or similar in nature. Every report made by a designated authority and every order passed by the designated member under this Chapter shall be dated and signed and sent to the noticee and also uploaded on the website

of SEBI. If the noticee is a member of a stock exchange, clearing corporation, a depository or a self-regulatory organization, a copy of the order shall also be sent to the concerned stock exchange, clearing corporation, depository or self regulatory organization.

SURRENDER OF ANY CERTIFICATE OF REGISTRATION

Regulation 31 provides that any person, who has been granted a certificate of registration under the Act or the regulations made thereunder, desirous of giving up its activity and surrender the certificate, may make a request for such surrender to SEBI and while disposing such request, SEBI shall not be bound by the procedure specified in the foregoing provisions of this Chapter.

- (a) the arrangements made by the person for maintenance and preservation of records and other documents required to be maintained under the relevant regulations;
- (b) redressal of investor grievances;
- (c) transfer of records, funds or securities of its clients;
- (d) the arrangements made by it for ensuring continuity of service to the clients;
- (e) defaults or pending action, if any.

While accepting surrender, SEBI may impose such conditions as it deems fit.

EFFECT OF DEBARMENT, SUSPENSION, CANCELLATION OR SURRENDER

Regulation 32 provides that on and from the date of debarment or suspension of the certificate, the concerned person shall –

- (a) not undertake any new assignment or contract or launch any new scheme and during the period of such debarment or suspension;
- (b) allow its clients or investors to withdraw or transfer their securities or funds without any additional cost to such client or investor;
- (c) make provisions as regards liability incurred or assumed by it;
- (d) take such other action including the action relating to any records or documents and securities or money of the investors.

On and from the date of surrender or cancellation of the certificate, the concerned person shall—

- (a) return the certificate of registration so cancelled to SEBI and shall not represent itself to be a holder of certificate for carrying out the activity for which such certificate had been granted;
- (b) cease to carry on any activity in respect of which the certificate had been granted;
- (c) transfer its activities to another person holding a valid certificate of registration to carry on such activity and allow its clients or investors to withdraw or transfer their securities or funds held in its custody or to withdraw any assignment given to it, without any additional cost to such client or investor;
- (d) make provisions as regards liability incurred or assumed by it;
- (e) take such other action including the action relating to any records or documents and securities or money of the investors.

APPEAL TO SECURITIES APPELLATE TRIBUNAL

Regulation 33 provides that the person aggrieved by an order under these regulations may prefer an appeal to the Securities Appellate Tribunal against such order in accordance with the provisions of section 15T of the Act and Rules prescribed in this regards.

PROCEDURE TO BE FOLLOWED UNDER THIS CHAPTER

Regulation 33B provides the procedure to be followed under this chapter are:-

- (1) The Chairman or member may appoint an officer of the Board, not below the rank of Assistant General Manager or Assistant Legal Advisor for giving his recommendation after following the procedure under this regulation in respect of the proceedings referred to in regulation 33A.

However, in respect of the proceedings referred to in regulation 33A, if a representation is received from an intermediary to dispense with the procedure laid down in regulation 33B, the Chairman or the member may not appoint an officer of the Board and pass an appropriate order after considering the representation of the intermediary.

- (2) The officer appointed shall issue to the intermediary, against whom the proceedings are being held, a notice requiring the intermediary to make a written submission in reply to the notice within such time, not exceeding 15 days after the receipt of the notice, as may be specified in the notice. However, the officer may extend the time for sufficient reasons to be recorded in writing.
- (3) If the intermediary fails to make a written submission to the notice within the period specified in the notice, the officer shall, after considering the circumstances and in light of the material on record, submit a report to the Chairman or the member, as the case may be, and may recommend taking of any action under regulation 27 as he considers appropriate in the circumstances of the case and shall give reasons for recommending such action.
- (4) If the intermediary makes submission within the said period, the officer shall, after considering the submission so made, submit a report to the Chairman or the member, as the case may be, and may recommend taking of any action under regulation 27 as he considers appropriate in the circumstances of the case and shall give reasons for recommending such action.
- (5) The Chairman or the member, as the case may be, after receipt of recommendations from the officer shall pass such orders as he may deem appropriate.
- (6) The Chairman or the member may pass a common order in respect of a number of intermediaries where the subject matter in question is substantially the same or similar in nature.

DIRECTIONS

As per regulation 35, SEBI can issue, necessary direction including but not limited to any or all of the following –

- (a) directing the intermediary or other persons associated with securities market to refund any money or securities collected from the investors under any scheme or otherwise, with or without interest;
- (b) directing the intermediary or other persons associated with securities market not to access the capital market or not to deal in securities for a particular period or not to associate with any intermediary or with any capital market related activity;
- (c) directing the recognised stock exchange concerned not to permit trading in the securities or units issued by a mutual fund or collective investment scheme;
- (d) directing the recognised stock exchange concerned to suspend trading in the securities or units issued by a mutual fund or collective investment scheme;
- (e) any other direction which SEBI may deem fit and proper.

Before issuing any directions, SEBI shall give a reasonable opportunity of being heard to the persons concerned. Further that if the circumstances warrant any interim direction is required to be passed immediately, SEBI shall give a reasonable opportunity of hearing to the persons concerned after passing the direction, without any undue delay.

RESEARCH ANALYSTS

“Research analyst” means a person who is primarily responsible for,-

- i. preparation or publication of the content of the research report; or
- ii. providing research report; or
- iii. making ‘buy/sell/hold’ recommendation; or
- iv. giving price target; or
- v. offering an opinion concerning public offer,

with respect to securities that are listed or to be listed in a stock exchange, whether or not any such person has the job title of ‘research analyst’ and includes any other entities engaged in issuance of research report or research analysis.

Explanation.-The term also includes any associated person who reports directly or indirectly to such a research analyst in connection with activities provided above;

Timely and accurate information about investment products is an important ingredient for making investment decisions. However, considering the volume and complexity of information it would be difficult for an investor for analyzing and grasping the information. In this context the Research Analysts play an important role. They study Companies and industries, analyze raw data, and make forecasts or recommendations about whether to buy, hold or sell securities. They analyze information to provide recommendations about investments in securities to their clients. Investors often view analysts as experts and important sources of information about the securities they review and often rely on their advice. There are basically three broad types of analysts, viz. sell-side analysts, buy-side analysts and independent analysts.

- **Sell-side Analysts-** They typically publish research reports on the securities of companies or industries that they cover. These Research reports carry specific recommendations, such as recommendation to buy, hold, or sell the subject security. It also includes the analyst’s expectation of the future price performance of the security (“price target”).
- **Buy-side Analysts-** They generally work for money managers like mutual funds, hedge funds, pension funds, or portfolio managers that purchase and sell securities for their own investment accounts or on behalf of others. Research reports of these analysts are generally circulated among the top management of the employer firms as these reports contain advice about which securities to buy, hold or sell.
- **Independent Analysts-** They work for research originators or boutique firms that are legal entities separate from full-service investment firms and sell their research to others on a subscription or other basis.

The activities of Research Analyst in India are governed by the SEBI (Research Analysts) Regulations, 2014.

SEBI (RESEARCH ANALYST) REGULATIONS, 2014

SEBI (Research Analyst) Regulations, 2014, were notified by SEBI on 1st September, 2014 in exercise of the powers conferred by section 30 of SEBI Act, 1992, SEBI made these regulations.

APPLICATION FOR GRANT OF CERTIFICATE

Regulation 3(1) provides that any person shall not act as a research analyst or research entity or hold itself out as a research analyst unless he has obtained a certificate of registration from SEBI under these regulations. Any person acting as research analyst or research entity before the commencement of these regulations may continue to do so for a period of six months from such commencement or, if it has made an application for a certificate of registration within the period of six months, till the disposal of such application.

Further that an investment adviser, credit rating agency, asset management company or fund manager, who issues research report or circulates/distributes research report to the public or its director or employee who makes public appearance, shall not be required to seek registration under regulation 3, subject to compliance of Chapter III of these regulations.

An application for grant of certificate of registration shall be made in Form A as specified in the First Schedule to these regulations and shall be accompanied by a non-refundable application fee to be paid in the manner specified in Second Schedule.

ISSUANCE OF RESEARCH REPORT BY A PERSON LOCATED OUTSIDE INDIA

Regulation 4 provides that any person located outside India engaged in issuance of research report or research analysis in respect of securities listed or proposed to be listed on a stock exchange shall enter into an agreement with a research analyst or research entity registered under these regulations.

Regulation 5 provides that SEBI may require the applicant to furnish further information or clarification for the purpose of consideration of the application. The applicant or his authorised representative, if so required, shall appear before SEBI for personal representation.

CONSIDERATION OF APPLICATION AND ELIGIBILITY CRITERIA

Regulation 6 lays down that SEBI shall take into account all matters which are relevant to the grant of certificate of registration. It shall assess whether:-

- (i) the applicant is an individual or a body corporate or limited liability partnership firm;
- (ii) in case the applicant is an individual, he is appropriately qualified and certified as specified in regulation 7.
- (iii) in case the applicant is a body corporate, the individuals employed as research analyst are qualified and certified as specified in regulation 7.
- (iv) in case the applicant is a partnership firm or a limited liability partnership, partners engaged in issuance of research report or research analysis are qualified and certified as specified in regulation 7.
- (v) in case the applicant is a research entity, the individuals employed as research analyst are qualified and certified as specified in regulation 7.
- (vi) the applicant fulfills the capital adequacy requirements.
- (vii) the applicant, individuals employed as research analyst and partners of the applicant, if any, are fit and proper persons.
- (viii) the applicant has the necessary infrastructure to effectively discharge the activities of research analyst;

- (ix) the applicant or any person directly or indirectly connected with the applicant has in the past been refused certificate by SEBI and if so, the grounds for such refusal;
- (x) any disciplinary action has been taken by SEBI or any other regulatory authority against the applicant or any person directly or indirectly connected to the applicant under the respective Act, rules or regulations made thereunder.

QUALIFICATION AND CERTIFICATION REQUIREMENT

Regulation 7 provides that an individual registered as research analyst, individuals employed as research analyst and partners of a research analyst, if any, engaged in preparation and/or publication of research report or research analysis shall have the following minimum qualifications:-

- (i) A professional qualification or post-graduate degree or post graduate diploma in finance, accountancy, business management, commerce, economics, capital market, financial services or markets provided by:
 - (a) a university which is recognized by University Grants Commission or by any other commission/ council/board/body established under an Act of Parliament in India for the purpose; or
 - (b) an institute/association affiliated with such university; or
 - (c) an institute/ association/university established by the central government or state government; or
 - (d) autonomous institute falling under administrative control of Government of India; or
- (ii) professional qualification or post-graduate degree or post graduate diploma which is accredited by All Indian Council for Technical Education, National Assessment and Accreditation Council or National Board of Accreditation or any other council/board/body set up under an Act of Parliament in India for the purpose; or
- (iii) a graduate in any discipline with an experience of at least five years in activities relating to financial products or markets or securities or fund or asset or portfolio management.

An individual registered as research analyst under these regulations, individuals employed as research analyst and partners of a research analyst, shall have, at all times, a NISM certification for research analysts as specified by SEBI or other certification recognized by SEBI from time to time. Research analyst or research entity already engaged in issuance of research report or research analysis seeking registration under these regulations shall ensure that it or the individuals employed by it as research analyst and/or its partners obtain such certification within two years from the date of commencement of these regulations.

CAPITAL ADEQUACY

Regulation 8 prescribe the capital adequacy requirement:-

- (1) of research analyst who is body corporate or limited liability partnership firm shall have a net worth of not less than twenty five lakh rupees.
- (2) of research analyst who is individual or partnership firm shall have net tangible assets of value not less than one lakh rupees.

All existing research analysts shall comply with the capital adequacy requirement within one year from the date of commencement of these regulations.

GRANT OF CERTIFICATE OF REGISTRATION

Regulation 9 stipulates that SEBI on being satisfied that the applicant is eligible, shall grant a certificate of registration in Form B under First Schedule after receipt of the payment of registration fees as specified in Second schedule and send intimation to the applicant in this regard.

The certificate of registration granted shall be valid till it is suspended or cancelled by SEBI.

RENEWAL OF CERTIFICATE

Regulation 11 provides that the research analyst who has already been granted certificate of registration by SEBI, prior to the commencement of the SEBI (Research Analysts) (Amendment) Regulations, 2016 shall be deemed to have been granted a certificate of registration, subject to payment of fee, as prescribed in Schedule II of these regulations.

PROCEDURE WHERE REGISTRATION IS REFUSED

Regulation 12 (1) lays down that after considering an application, if SEBI is of the opinion that a certificate should not be granted to the applicant, it may reject the application after giving the applicant a reasonable opportunity of being heard.

The decision of SEBI rejecting the application shall be communicated to the applicant within thirty days of such decision. Where an application for a certificate is rejected by SEBI, the applicant shall forthwith cease to act as a research analyst.

CONDITIONS OF CERTIFICATE

Regulation 13 provides that the certificate granted under regulation 9 shall, inter alia, be subject to the following conditions:-

- (i) the research analyst shall abide by the provisions of the Act and these regulations;
- (ii) the research analyst shall forthwith inform SEBI in writing, if any information or particulars previously submitted to SEBI are found to be false or misleading in any material particular or if there is any material change in the information already submitted;
- (iii) research analyst registered under these regulations shall use the term "research analyst" in all correspondences with its clients.

RECOGNITION OF BODY OR BODY CORPORATE FOR REGULATION OF RESEARCH ANALYSTS

Regulation 14 provides that SEBI may recognize any body or body corporate for the purpose of regulating research analysts. SEBI may, at the time of recognition of such body or body corporate, delegate administration, supervision and regulation of research analysts to such body or body corporate on such terms and conditions as may be specified by SEBI.

SEBI may also specify that any person shall not act as research analyst unless he is a member of a recognized body or body corporate.

ESTABLISHING INTERNAL POLICIES AND PROCEDURES

Regulation 15 provides that research analyst or research entity shall have written internal policies and control procedures governing the dealing and trading by any research analyst for:

- (i) addressing actual or potential conflict of interest arising from such dealings or trading of securities of subject company;
- (ii) promoting objective and reliable research that reflects the unbiased view of research analyst; and
- (iii) preventing the use of research report or research analysis to manipulate the securities market.

Research analyst or research entity shall have in place appropriate mechanisms to ensure independence of its research activities from its other business activities.

LIMITATIONS ON TRADING BY RESEARCH ANALYSTS

Regulation 16 lays down the following limitations on trading by research analyst:-

- (1) Personal trading activities of the individuals employed as research analyst by research entity shall be monitored, recorded and where ever necessary, shall be subject to a formal approval process.
- (2) Independent research analysts, individuals employed as research analyst by research entity or their associates shall not deal or trade in securities that the research analyst recommends or follows within thirty days before and five days after the publication of a research report.
- (3) Independent research analysts, individuals employed as research analysts by research entity or their associates shall not deal or trade directly or indirectly in securities that he reviews in a manner contrary to his given recommendation.
- (4) Independent research analysts, individuals employed as research analysts by research entity or their associate shall not purchase or receive securities of the issuer before the issuer's initial public offering, if the issuer is principally engaged in the same types of business as companies that the research analyst follows or recommends.
- (5) Provisions of sub-regulations (2) to (4) shall apply mutatis mutandis to a research entity unless it has segregated its research activities from all other activities and maintained an arms-length relationship between such activities.
- (6) Notwithstanding anything contained in sub-regulations (2) to (4), such restrictions to trade or deal in securities may not apply in case of significant news or event concerning the subject company or based upon an unanticipated significant change in the personal financial circumstances of the research analyst, subject to prior written approval as per the terms specified in the approved internal policies and procedures.

COMPENSATION OF RESEARCH ANALYSTS

Regulation 17 provides the compensation of research analysts:-

- (1) Research entity shall not pay any bonus, salary or other form of compensation to any individual employed as research analyst that is determined or based on any specific merchant banking or investment banking or brokerage services transaction.
- (2) The compensation of all individuals employed as research analyst shall be reviewed, documented and approved annually by board of directors/committee appointed by board of directors of the research entity, which does not consist of representation from its merchant banking or investment banking or brokerage services divisions.
- (3) The board of directors/committee appointed by board of directors of the research entity approving or reviewing the compensation of individual employed as research analyst shall not take into account such individual's contribution to the research entity's investment banking or merchant banking or brokerage services business.
- (4) An individual employed as research analyst by research entity shall not be subject to the supervision or control of any employee of the merchant banking or investment banking or brokerage services divisions of that research entity.

LIMITATIONS ON PUBLICATION OF RESEARCH REPORT, PUBLIC APPEARANCE AND CONDUCT OF BUSINESS, ETC.

Regulation 18 provides the following limitations on publication of research report, public appearance and conduct of business.

- (1) Research analyst or research entity shall not publish or distribute research report or research analysis or make public appearance regarding a subject company for which he has acted as a manager or co-manager at any time falling within a period of:
 - (a) Forty days immediately following the day on which the securities are priced if the offering is an initial public offering; or
 - (b) Ten days immediately following the day on which the securities are priced if the offering is a further public offering.

Research analyst or research entity may publish or distribute research report or research analysis or make public appearance within such forty day and ten day periods, subject to prior written approval of legal or compliance personnel as specified in the internal policies and procedures.

- (2) A research entity who has agreed to participate or is participating as an underwriter of an issuer's initial public offering shall not publish or distribute a research report or make public appearance regarding that issuer before expiry of twenty five days from the date of the offering.
- (3) Research analyst or research entity who has acted as a manager or co-manager of public offering of securities of a company shall not publish or distribute a research report or make a public appearance concerning that company within fifteen days prior to date of entering into and fifteen days after the expiration/waiver/termination of a lock-up agreement or any other agreement that the research analyst or research entity has entered into with a subject company that restricts or prohibits the sale of securities held by the subject company after the completion of public offering of securities.

Research analyst or research entity may publish or distribute research report or research analysis or make public appearance regarding that company within such fifteen days subject to prior written approval of legal or compliance personnel as specified in the internal policies and procedures.

- (4) Research analyst or individuals employed as research analyst by research entity shall not participate in business activities designed to solicit investment banking or merchant banking or brokerage services business, such as sales pitches and deal road shows.
- (5) Research analyst or individuals employed as research analyst by research entity shall not engage in any communication with a current or prospective client in the presence of personnel from investment banking or merchant banking or brokerage services divisions or company management about an investment banking services transaction.
- (6) Investment banking or merchant banking or brokerage services division's personnel of research entity shall not direct the individuals employed as research analyst to engage in sales or marketing related to an investment banking or merchant banking or brokerage services and shall not direct the research analyst to engage in any communication with a current or prospective client about such division's transaction.

However, sub-regulations (4) to (6) shall not prohibit research analyst or research entity from engaging in investor education activities including publication of pre-deal research and briefing the views of the research analyst on the transaction to the sales or marketing personnel.

- (7) Research analyst or research entity shall have adequate documentary basis, supported by research, for preparing a research report.
- (8) Research analyst or research entity shall not provide any promise or assurance of favourable review in its research report to a company or industry or sector or group of companies or business group as consideration to commence or influence a business relationship or for the receipt of compensation or other benefits.

- (9) Research analyst or research entity shall not issue a research report that is not consistent with the views of the individuals employed as research analyst regarding a subject company.
- (10) Research entity shall ensure that the individuals employed as research analyst are separate from other employees who are performing sales trading, dealing, corporate finance advisory or any other activity that may affect the independence of its research report.

However, the individual employed as research analyst by research entity can receive feedback from sales or trading personnel of brokerage division to ascertain the impact of research report.

DISCLOSURES IN RESEARCH REPORTS

Regulation 19 stipulates that a research analyst or research entity shall disclose all material information about itself including its business activity, disciplinary history, the terms and conditions on which it offers research report, details of associates and such other information as is necessary to take an investment decision, including the following:

- (i) Research analyst or research entity shall disclose the following in research report and in public appearance with regard to ownership and material conflicts of interest:
 - (a) whether the research analyst or research entity or his associate or his relative has any financial interest in the subject company and the nature of such financial interest;
 - (b) whether the research analyst or research entity or its associates or relatives, have actual/beneficial ownership of 1 per cent or more securities of the subject company, at the end of the month immediately preceding the date of publication of the research report or date of the public appearance;
 - (c) whether the research analyst or research entity or his associate or his relative, has any other material conflict of interest at the time of publication of the research report or at the time of public appearance;
- (ii) Research analyst or research entity shall disclose the following in research report with regard to receipt of compensation:
 - (a) whether it or its associates have received any compensation from the subject company in the past twelve months;
 - (b) whether it or its associates have managed or co-managed public offering of securities for the subject company in the past twelve months;
 - (c) whether it or its associates have received any compensation for investment banking or merchant banking or brokerage services from the subject company in the past twelve months;
 - (d) whether it or its associates have received any compensation for products or services other than investment banking or merchant banking or brokerage services from the subject company in the past twelve months;
 - (e) whether it or its associates have received any compensation or other benefits from the subject company or third party in connection with the research report.
- (iii) Research analyst or research entity shall disclose the following in public appearance with regard to receipt of compensation:
 - (a) whether it or its associates have received any compensation from the subject company in the past twelve months;
 - (b) whether the subject company is or was a client during twelve months preceding the date of distribution of the research report and the types of services provided.

However, research analyst or research entity shall not be required to make a disclosure as per sub-clauses (c), (d) and (e) of clause (ii) or sub-clauses (a) and (b) of clause (iii) to the extent such disclosure would reveal material non-public information regarding specific potential future investment banking or merchant banking or brokerage services transactions of the subject company.

- (iv) whether the research analyst has served as an officer, director or employee of the subject company;
- (v) whether the research analyst or research entity has been engaged in market making activity for the subject company;
- (vi) Research analyst or research entity shall provide all other disclosures in research report and public appearance as specified by SEBI under any other regulations.

CONTENTS OF RESEARCH REPORT

Regulation 20 stipulates the following contents of research report:-

- (1) Research analyst or research entity shall take steps to ensure that facts in its research reports are based on reliable information and shall define the terms used in making recommendations, and these terms shall be consistently used.
- (2) Research analyst or research entity that employs a rating system must clearly define the meaning of each such rating including the time horizon and benchmarks on which a rating is based.
- (3) If a research report contains either a rating or price target for subject company's securities and the research analyst or research entity has assigned a rating or price target to the securities for at least one year, such research report shall also provide the graph of daily closing price of such securities for the period assigned or for a three-year period, whichever is shorter.

DISTRIBUTION OF RESEARCH REPORTS

Regulation 22 provides the following distribution of Research Report:-

- (1) A research report shall not be made available selectively to internal trading personnel or a particular client or class of clients in advance of other clients who are entitled to receive the research report.
- (2) Research analyst or research entity who distributes any third party research report shall review the third party research report for any untrue statement of material fact or any false or misleading information.
- (3) Research analyst or research entity who distributes any third party research report shall disclose any material conflict of interest of such third party research provider or he shall provide a web address that directs a recipient to the relevant disclosures.
- (4) This shall not apply to a research analyst or research entity if he has no direct or indirect business or contractual relationship with such third party research provider.

ADDITIONAL DISCLOSURES BY PROXY ADVISER

Regulations 23 provides that all the provisions of Chapter II, III, IV, V and VI shall apply mutatis mutandis to the proxy adviser. The employees of proxy advisors engaged in providing proxy advisory services shall be required to have a minimum qualification of being a graduate in any discipline. Further that certification requirements for employees of proxy advisors engaged in providing proxy advisory services shall be as specified by SEBI.

The time period for compliance with capital adequacy for proxy advisors shall be three years. The proxy adviser shall additionally disclose the following:

- (i) the extent of research involved in a particular recommendation and the extent and/or effectiveness of its controls and procedures in ensuring the accuracy of issuer data;

- (ii) policies and procedures for interacting with issuers, informing issuers about the recommendation and review of recommendations;

Proxy adviser shall maintain the record of his voting recommendations and furnish the same to SEBI on request. In case of any inconsistency or difficulty in respect of applicability of provisions of these regulations to proxy advisers, SEBI may issue such clarifications or exemptions as may be deemed appropriate.

GENERAL RESPONSIBILITY

Regulation 24 provides the following responsibility of research analyst or research entity:-

- (1) Research analyst or research entity shall maintain an arms-length relationship between its research activity and other activities.
- (2) Research analyst or research entity shall abide by Code of Conduct as specified in Third Schedule.
- (3) In case of change in control of the research analyst or research entity, prior approval from SEBI shall be taken.
- (4) Research analyst or research entity shall furnish to SEBI information and reports as may be specified by SEBI from time to time.
- (5) It shall be the responsibility of the research analyst or research entity to ensure that its employees or partners, as may be applicable, comply with the certification and qualification requirements under regulation 7 at all times.

MAINTENANCE OF RECORDS

Regulation 25(1) lays down that the research analyst or research entity shall maintain the following records:

- (i) research report duly signed and dated;
- (ii) research recommendation provided;
- (iii) rationale for arriving at research recommendation;
- (iv) record of public appearance.

All records shall be maintained either in physical or electronic form and preserved for a minimum period of five years. Where records are required to be duly signed and are maintained in electronic form, such records shall be digitally signed. Research analyst or research entity shall conduct annual audit in respect of compliance with these regulations from a member of Institute of Chartered Accountants of India or Institute of Company Secretaries of India.

APPOINTMENT OF COMPLIANCE OFFICER

Regulation 26 provides that every research analyst or research entity which is a body corporate or limited liability partnership firm shall appoint a compliance officer who shall be responsible for monitoring the compliance of the provisions of the Act, these regulations and circulars issued by SEBI.

INSPECTION

SEBI may appoint one or more persons as inspecting officer to undertake inspection of the books of accounts, records and documents relating to research analyst or research entity for any of the following purpose :-

- (i) to ensure that the books of account, records and documents are being maintained in the manner specified in these regulations;
- (ii) to inspect into complaints received from any person, on any matter having a bearing on the activities of a research analyst;

- (iii) to ascertain whether the provisions of the Act and these regulations are being complied with by the research analyst or research entity;
- (iv) to inspect into the affairs of research analyst or research entity in relation to research activities, in the interest of the securities market or in the interest of investors.

OBLIGATION OF RESEARCH ANALYST ON INSPECTION

It is the duty of every research analyst or research entity whose affairs are being inspected and any other associate person who is in possession of relevant information, to produce to the inspecting authority such books, accounts and other documents in his custody or control and furnish him with such statements and information as the inspecting authority may require for the purposes of inspection.

It is the duty of research analyst or research entity and any other associate person, to give to the inspecting authority all such assistance and shall extend all such co-operation as may be required in connection with the inspection and shall furnish such information as sought by the inspecting authority in connection with the inspection.

The inspecting authority shall, for the purposes of inspection, have power to examine on oath and record the statement of any employee, director, partner or person responsible for or connected with the activities of research analyst or research entity or any other associate person having relevant information pertaining to such research analyst or research entity. The inspecting authority shall, for the purposes of inspection, have power to obtain authenticated copies of documents, books, accounts of research analyst or research entity, from any person having control or custody of such documents, books or accounts.

SUBMISSION OF REPORT TO SEBI

The inspecting authority shall, as soon as possible, on completion of the inspection submit an inspection report to SEBI and if directed to do so by SEBI, the inspecting authority may submit an interim report.

ACTION ON THE INSPECTION REPORT

SEBI may after consideration of the inspection report and after giving reasonable opportunity of hearing to research analyst or research entity or its authorized representatives, without prejudice to any other action under the Act, issue such directions as it deems fit in the interest of securities market or the investors including requiring research analyst or research entity not to provide research recommendation for a particular period;

- (i) requiring the research analyst or research entity to refund any money collected as fees, charges or commissions or otherwise to the concerned clients along with the requisite interest.
- (ii) prohibiting the research analyst or research entity from operating in the capital market or accessing the capital market for a specified period.

LIABILITY FOR ACTION IN CASE OF DEFAULT

Regulation 32 stipulates the provisions for liability for action in case of default. A Research analyst or research entity who:

- (i) contravenes any of the provisions of the Act or any regulations or circulars issued thereunder;
- (ii) fails to furnish any information relating to its activity as a research analyst as required by SEBI;
- (iii) furnishes to SEBI information which is false or misleading in any material particular;
- (iv) does not submit periodic returns or reports as required by SEBI;
- (v) does not co-operate in any enquiry, inspection or investigation conducted by SEBI;

- (vi) fails to resolve the complaints or fails to give a satisfactory reply to SEBI in this behalf, shall be dealt with in the manner provided under the Act or SEBI (Intermediaries) Regulations, 2008.

SEBI {KYC (KNOW YOUR CLIENT) REGISTRATION AGENCY (KRA)}, REGULATIONS, 2011

With a view to bring uniformity in the KYC requirements for the securities markets, SEBI has initiated usage of uniform KYC by all SEBI registered intermediaries. In this regard SEBI has issued the SEBI {KYC (Know Your Client) Registration Agency (KRA)}, Regulations, 2011.

KRA provides for centralization of the KYC records in the securities market. The client who is desirous of opening an account/trade/deal with the SEBI registered Intermediary shall submit the KYC details through the KYC Registration form and supporting documents. The Intermediary shall perform the initial KYC and upload the details on the system of the KYC Registration Agency (KRA). This KYC information can be accessed by all the SEBI Registered Intermediaries while dealing with the same client. As a result, once the client has done KYC with a SEBI registered intermediary, he need not undergo the same process again with another intermediary.

The key highlights of the regulation are as follows:

- An intermediary shall perform the initial KYC of its clients and upload the details on the system of the KRA.
- When the client approaches another intermediary, the intermediary can verify and download the client's details from the system of the KRA (KYC Registration Agency).
- As a result, once the client has done KYC with a SEBI registered intermediary, he need not undergo the same process again with another intermediary.
- SEBI shall not consider an application, unless the applicant is a fit and proper person to the satisfaction of the SEBI and is a wholly-owned subsidiary of a recognised stock exchange, having nationwide network of trading terminals
- Besides, wholly-owned subsidiaries of depositories, other market intermediaries and Self Regulatory Organisations would also be able to secure certificate for initial registration as KRA..
- The KRA shall obtain the KYC documents of the client from the intermediary as prescribed by SEBI and in terms of the rules, regulations, guidelines and circulars issued by SEBI or any other authority for Prevention of Money Laundering, from time to time.
- The KRAs can, in coordination with each other, prepare operating instructions for implementing requirements under this regulation and share data on KYC documents.
- KRA shall be responsible for storing, safeguarding and retrieving the KYC documents and submit to SEBI or any other statutory authority as and when required.

LIST OF SEBI REGISTERED INTERMEDIARIES

List of SEBI registered intermediaries as per the new KYC Regulations

1. KYC Registration Agencies (KRAs),
2. Stock Brokers through Stock Exchanges,
3. Depository Participants (DPs) through Depositories,
4. Mutual Funds (MFs)
5. Portfolio Managers (PMs)
6. Venture Capital Funds (VCFs)
7. Collective Investment Schemes (CIS)

GRANT OF CERTIFICATE OF REGISTRATION

SEBI on being satisfied that the applicant is eligible, shall send intimation to that effect to the applicant, for the grant of certificate of registration, and grant a certificate in the Form as specified by SEBI. The KRA which has already been granted certificate of registration by SEBI, prior to the commencement of the SEBI (Change in Conditions of Registration of Certain Intermediaries) (Amendment) Regulations, 2016 shall be deemed to have been granted a certificate of registration, in terms of these regulation. The certificate of registration granted shall be valid unless it is suspended or cancelled by SEBI. The grant of certificate of registration shall be subject to the payment of such fees and in such manner as specified in these regulations. The KRA shall immediately intimate SEBI, details of changes that have taken place in the information that was submitted, while seeking registration.

CRITERIA FOR FIT AND PROPER PERSON

For the purpose of determining whether an applicant is a fit and proper person, SEBI may take into account the criteria specified in SEBI (Intermediaries) Regulations.

CODE OF CONDUCT

The KRA holding a certificate of registration shall at all times abide by the Code of Conduct as specified in Schedule III of these regulations.

DOCUMENTS TO BE OBTAINED BY THE KRA FOR THE PURPOSE OF KYC

The KRA shall obtain the KYC documents of the client from the intermediary; as prescribed by SEBI and in terms of the rules, regulations, guidelines and circulars issued by SEBI or any other authority for Prevention of Money Laundering, from time to time.

FUNCTIONS AND OBLIGATIONS OF THE KRA

The KRA has the following functions and obligations –

- (a) KRA may prepare the Operating Instructions in co-ordination with other KRA(s) and issue the same to implement the requirements of these regulations.
- (b) KRA(s) shall have electronic connectivity and with other KRA(s) in order to establish inter-operability among KRAs.
- (c) KRA shall have a secure data transmission link with other KRA(s) and with each intermediary that uploads the KYC documents on its system and relies upon its data.
- (d) KRA shall be responsible for storing, safeguarding and retrieving the KYC documents and submit to SEBI or any other statutory authority as and when required.
- (e) KRA shall retain the KYC documents of the client, in electronic form for the period specified by Rules, as well as ensuring that retrieval of KYC information is facilitated within stipulated time period.
- (f) Any information updated about a client shall be disseminated by KRA to all intermediaries that avail of the services of the KRA in respect of that client.
- (g) KRA shall ensure that the integrity of the automatic data processing systems for electronic records is maintained at all times.
- (h) KRA shall take all precautions necessary to ensure that the KYC documents/records are not lost, destroyed or tampered with and that sufficient back up of electronic records is available at all times at a different place.

- (i) KRA shall have adequate mechanisms for the purposes of reviewing, monitoring and evaluating its controls, systems, procedures and safeguards.
- (j) KRA shall cause an audit of its controls, systems, procedures and safeguards to be carried out periodically and take corrective actions for deficiencies, if any and report to SEBI.
- (k) KRA shall take all reasonable measures to prevent unauthorized access to its database and have audit of its systems and procedures at regular intervals as prescribed by SEBI.
- (l) KRA shall have checks built in its system so that an intermediary can access the information only for the clients who approach him.
- (m) KRA shall appoint a compliance officer who shall be responsible for monitoring the compliance of the Act, rules and regulations, notifications, guidelines, instructions, etc., issued by SEBI or the Central Government and for redressal of client's grievances. The compliance officer shall immediately and independently report to SEBI any non-compliance observed by him.
- (n) KRA shall send a letter to each client after receipt of the KYC documents from the intermediary, confirming the client's details thereof.
- (o) KRA shall take adequate steps for redressal of the grievances of the clients within one month of the date of receipt of the complaint and keep the SEBI informed about the number, nature and other particulars of the complaints from such investors.

FUNCTIONS AND OBLIGATIONS OF AN INTERMEDIARY

The Intermediary has the following functions and obligations –

- (a) The intermediary shall perform the initial KYC/due diligence of the client, upload the KYC information with proper authentication on the system of the KRA, furnish the scanned images of the KYC documents to the KRA, and retain the physical KYC documents.

However, in case of clients of a mutual fund, the Registrar to an Issue and Share Transfer Agent appointed by the mutual fund may perform the initial KYC/due diligence of the client, upload the KYC information with proper authentication on the system of the KRA, and furnish the scanned images of KYC documents to the KRA.

- (b) The intermediary or the mutual fund, as the case may be, shall furnish the physical KYC documents or authenticated copies thereof to the KRA, whenever so desired by the KRA.
- (c) When the client approaches another intermediary subsequently, the intermediary shall verify and download the client's details from the system of KRA.

However, upon receipt of information on change in KYC details and status of the clients by the intermediary or when it comes to the knowledge of the intermediary, at any stage, the intermediary shall be responsible for uploading the updated information on the system of KRA and retaining the physical documents.

- (d) An intermediary shall not use the KYC data of a client obtained from the KRA for purposes other than it is meant for; nor shall it make any commercial gain by sharing the same with any third party including its affiliates or associates.
- (e) The intermediary shall have the ultimate responsibility for the KYC of its clients, by undertaking enhanced KYC measures commensurate with the risk profile of its clients.

LIABILITY FOR ACTION IN CASE OF DEFAULT

A KRA shall be liable for action if it –

- (a) contravenes any of the provisions of the Act, and these regulations;
- (b) fails to furnish any information relating to its activity as a KRA as required under these regulations;
- (c) does not co-operate in any inspection or investigation or enquiry conducted by SEBI;
- (d) fails to comply with any direction of SEBI;
- (e) fails to pay the requisite fees to SEBI;

and shall be dealt with in the manner provided under the SEBI (Intermediaries) Regulations.

IN-PERSON VERIFICATION (IPV)

SEBI has made it compulsory for all the intermediaries to carry out IPV of their clients.

The intermediary shall ensure that the details like name of the person doing IPV, his designation, organization with his signatures and date are recorded on the KYC form at the time of IPV.

The IPV carried out by one SEBI registered intermediary can be relied upon by another intermediary.

In case of Stock brokers, their sub-brokers or Authorised Persons (appointed by the stock brokers after getting approval from the concerned Stock Exchanges) can perform the IPV.

In case of Mutual Funds, their Asset Management Companies (AMCs) and the distributors who comply with the certification process of National Institute of Securities Market (NISM) or Association of Mutual Funds (AMFI) and have undergone the process of 'Know Your Distributor (KYD)', can perform the IPV.

However, in case of applications received by the mutual funds directly from the clients i.e. not through any distributor), they may also rely upon the IPV performed by the scheduled commercial banks.

SEBI (SELF REGULATORY ORGANISATIONS) REGULATIONS, 2004

SEBI (Self Regulatory Organizations) Regulations, 2004 came into effect on 19th February, 2004.

RECOGNITION OF SELF REGULATORY ORGANIZATION

Regulation 3 provides that any group or association of intermediaries, which is desirous of being recognized as a Self Regulatory Organization, may form a company under section 8 of the Companies Act, 2013 and such company may make an application to the SEBI for grant of certificate of recognition as a Self Regulatory Organization. However, a distributors shall be deemed to be any intermediary for the purpose of this regulation.

Further, SEBI may, in case of distributors engaged by asset management companies of mutual funds, grant certificate of recognition to only one group of association making in application under this regulation.

Every application made by such company must contain such particulars as may be specified and is to be accompanied by a copy of the governing norms of Self Regulatory Organization and also a copy of the memorandum and articles of association relating in general to the constitution of the Self Regulatory Organization and in particular, to –

- (a) Board of Directors of Self Regulatory Organization, its constitution and powers of management and the manner in which its business would be transacted;
- (b) the powers and duties of the office bearers of Self Regulatory Organization;

- (c) the admission into the Self Regulatory Organization of members, agents, their qualifications for membership, and the exclusion, suspension, expulsion and readmission of members therefrom or there into;

The application is to be signed on behalf of the applicant under authority of its Board of Directors by its Chairman, Managing Director, Chief Executive Officer or whole time director. The application is to be made in Form A of the first schedule and is to be accompanied by a non-refundable application fee, as specified in Part A of the second schedule, to be paid in the manner specified in Part B thereof.

ELIGIBILITY CRITERIA

Regulation 4 provides the following criteria to be fulfilled by an association seeking registration under these regulations:-

- (a) the applicant should have been granted license under section 8 of Companies Act, 2013;
- (b) the memorandum of association, should specify admission of members and discharging the functions of Self Regulatory Organization as one of its main objects;
- (c) the applicant should have a minimum networth of one crore rupees;
- (d) the applicant is to have adequate infrastructure, to enable it to discharge its functions as a Self Regulatory Organization in accordance with the provisions of the Act and these regulations;
- (e) the directors have the professional competence, financial soundness and general reputation of fairness and integrity to the satisfaction of SEBI;
- (f) neither the applicant, nor any director of the applicant is involved in any legal proceeding connected with the securities market, which may have an adverse impact on the interests of the investors;
- (g) neither the applicant, nor any director has at any time in the past been convicted of any offence involving moral turpitude or any economic offence;
- (h) the applicant has, in its employment, persons having adequate professional and other relevant experience to the satisfaction of SEBI;
- (i) the applicant, is a fit and proper person based on the internal specified in Schedule II of SEBI (Intermediaries) Regulations, 2008;
- (j) grant of certificate to the applicant is in the interest of investors and the securities market.

GRANT OF IN-PRINCIPLE APPROVAL

Regulation 4A stipulates that where the applicant is not in compliance with the provisions of clauses (c), (d) or (h) of regulation 4, on the date of submission of the application under regulation 3, SEBI may grant an in-principle approval to the applicant, which shall be valid for a period of one hundred and eighty days, within which the applicant shall ensure compliance with all provisions of regulation 4.

However, SEBI may, upon sufficient cause shown by the applicant, extend the validity of the in-principle approval for a further period not exceeding ninety days.

GRANT OF RECOGNITION AS A SELF REGULATORY ORGANIZATION

If SEBI is satisfied, after making such inquiry as may be necessary in this behalf and after obtaining such further information, if any, as it may require, –

- (a) that the articles and governing norms of the applicant applying for recognition are in conformity with such conditions as may be specified by SEBI;
- (b) that the applicant is willing to comply with any other conditions which SEBI may impose for the purpose of carrying out the objects of these Regulations; and,
- (c) that it would be in the interest of the trade and also in the public interest to grant recognition to the applicant as a Self Regulatory Organization;

SEBI may grant certificate of recognition to the applicant as a Self Regulatory Organization in Form B1 of the First Schedule subject to such terms and conditions as it may deem fit and appropriate.

Regulation 5(2) empowers SEBI to specify any conditions for the grant of recognition to the applicant as a Self Regulatory Organization. Such conditions may relate to –

- (i) the qualification for membership of the Self Regulatory Organization;
- (ii) the representation of SEBI in the Board of Directors of the Self Regulatory Organization by such number of directors not exceeding four as SEBI may nominate in this behalf; and
- (iii) the maintenance of accounts of members and their audit by chartered accountants whenever such audit is required by SEBI.

The Self Regulatory Organization cannot amend its articles without the prior written approval of the SEBI.

APPLICATION TO CONFORM TO THE REQUIREMENTS

Regulation 6 provides that subject to provisions of regulation 4A, any application for a certificate, which is not complete in all respects or does not conform to the requirements of these regulations and particularly regulations 3, 4 and 5 or instructions specified in Form A shall be rejected by SEBI. However, before rejecting any such application, SEBI shall give an opportunity to the applicant to remove such objections as may be indicated by SEBI, within 30 days of the date of receipt of relevant communication, from SEBI. On sufficient cause being shown, SEBI may extend the time for removal of objections by such further time, not exceeding 30 days as it may consider fit, to enable the applicant to remove such objections.

FURNISHING OF INFORMATION, CLARIFICATION AND PERSONAL REPRESENTATION

SEBI may under Regulation 7 require the applicant to furnish such further information or clarification as it may consider necessary for the purpose of processing of the application. It may also require the applicant to appear before it through an authorized representative for personal representation in connection with the grant of a certificate of recognition.

CONDITIONS OF CERTIFICATE AND VALIDITY PERIOD

As provided under Regulation 8, the certificate granted under regulation 5 is valid for a period of five years, and subject to the following conditions, namely: -

- (a) the applicant shall comply with the provisions of the Act, applicable regulations and guidelines, directions or circulars issued by the SEBI from time to time;
- (b) any information or particulars furnished to the SEBI by the applicant shall not be false or misleading in any material respect;
- (c) where any material information or particulars furnished to SEBI by the applicant, in or in connection with the application for recognition, has undergone change subsequent to its furnishing, the applicant shall forthwith inform the fact to SEBI in writing.

RENEWAL OF CERTIFICATE

Regulation 9 provides that an application for renewal of Certificate of Recognition shall make an application to SEBI in Form A of the First Schedule. Such application shall be made not less than three months before expiry of the period of validity of the certificate. The application shall be accompanied by a renewal fee as specified in the second schedule and, as far as may be, shall be dealt with in the same manner as if it were an application for the grant of a fresh certificate under regulation 3.

SEBI, if satisfied may renew the certificate in Form B2 of the First Schedule subject to such terms and conditions as it may deem fit and appropriate.

PROCEDURE WHERE CERTIFICATE IS NOT GRANTED

Regulation 10 provides that if, after considering an application SEBI is of the opinion that a certificate should not be granted or renewed, it may, after giving the applicant a reasonable opportunity of being heard, reject the application within a period of thirty days of receipt of such application complete in all respects or within thirty days of receipt of further information or clarification sought. The fact of the rejection of the application shall be communicated to the applicant forthwith stating the grounds for such rejection.

EFFECT OF REFUSAL TO GRANT CERTIFICATE

Regulation 11 provides that an applicant whose application for the grant of a certificate has been rejected shall not undertake any activity as Self Regulatory Organization. Similarly, a Self Regulatory Organization whose application for the renewal of certificate has been rejected by SEBI shall on and from the date of the receipt of the communication of rejection from SEBI cease to carry on any activity as Self Regulatory Organization.

If SEBI is satisfied that it is in the interests of investors to do so, it may permit Self Regulatory Organization to complete the functions or obligations already initiated or undertaken by it during the pendency of the application or during the period of validity of the certificate. In order to protect the interests of investors, SEBI may issue directions with regard to the transfer of records, documents or reports relating to the functions of the Self Regulatory Organization, whose application for the grant or renewal of a certificate has been rejected. Further, SEBI may, appoint any person to take charge of the records, documents or reports relating to the organization and also determine the terms and conditions of such appointment.

COMPOSITION OF BOARD OF DIRECTORS

Regulation 12 of Chapter III of the Regulations provides that the Articles of Association of a Self Regulatory Organization shall provide for the following: –

- (a) There shall be a Board of Directors of the Self Regulatory Organization and majority of directors shall be independent directors.
- (b) The independent directors shall not be required to hold any qualification shares.
- (c) The Board of Directors shall consist of nine directors out of which five directors shall be nominated by SEBI and the remaining four shall be elected by the members of the Self Regulatory Organization.
- (d) The General Superintendence, direction and management of the affairs of the Self Regulatory Organization shall vest in its Board of Directors, which may exercise all powers and do all acts and things which may be exercised or done by the Self Regulatory Organization.
- (e) There shall be a Chairman, who shall be an independent professional, appointed by Board of Directors, with the prior approval of SEBI.

- (f) The Chairman shall be responsible for day-to-day administration of Self Regulatory Organization and implementing the decisions of Board of Directors.
- (g) The Board of Directors may establish committees including disciplinary committee, screening committee, arbitration committee or remuneration committee in order to carry out the purposes of these regulations. It has been provided that the committees constituted under this regulation may consist wholly of other persons or partly of directors and partly of other persons. The majority of members of each such committee shall be independent.
- (h) The office bearers of Board of Directors shall relinquish their office, when SEBI passes an order under clause (c) of sub-section (4) of section 11 of the SEBI Act.
- (i) The Board of Directors of the Self Regulatory Organization shall be reconstituted as and when required by SEBI.

MEMBERSHIP OF SELF REGULATORY ORGANIZATION

As per Regulation 13, any application for registration or renewal of registration as an intermediary with SEBI under the respective regulations applicable to such intermediaries, shall in case of any applicant who is a member of a Self Regulatory Organization or who ought to be a member of a Self Regulatory Organization, be made only through the Self Regulatory Organization of which he is a member, in the specified manner. The application is to be forwarded by the Self Regulatory Organization to SEBI along with its recommendation for grant or refusal of certificate of registration not later than 30 days from the date of its receipt. The Self Regulatory Organization is also required to give the reasons for its recommendation either for granting certificate of recognition or for refusal of certificate of registration by SEBI.

FUNCTIONS AND OBLIGATIONS OF SELF REGULATORY ORGANIZATION

As per Regulation 14, a Self Regulatory Organization shall always abide by the directions of SEBI. It shall be responsible for investor protection and education of investors or its members and shall ensure observance of Securities Laws by its members. It is required to specify standard of conduct for its members and also shall be responsible for the implementation of the same by its members. The SRO is required to conduct inspection and audit of its members, on regular basis, through independent auditors. The Annual Report of the SRO is to be submitted to SEBI. The SRO shall treat all its members and the applications for membership in a fair and transparent manner. The SRO may collect admission and membership fees from its members for carrying out the purposes of these regulations. SEBI is to be promptly informed of violations of the provisions of the Act, the rules, the regulations, the directions, the circulars or the guidelines by any of its members. The SRO is required to conduct screening and certification tests for its members, agents and such other persons as it may determine. The SRO is to conduct training programmes for its members or agents and also conduct awareness programmes for securities market investors. The SRO is required to make endeavors for introduction of best business practices amongst its members. It must act in utmost good faith and must avoid conflict of interest in the conduct of its functions. The SRO must comply with the norms of corporate governance as applicable to listed companies. It may discharge such other functions and obligations as may be specified by SEBI, from time to time.

GOVERNING NORMS OF SELF REGULATORY ORGANIZATION

Regulation 15 provides that a Self Regulatory Organization may, subject to the previous approval of SEBI, make governing norms and articles consistent with the provisions of the Act and these regulations. In particular, and without prejudice to the generality of the foregoing power, the governing norms or articles may provide for:

- (i) eligibility criteria for admission and removal of members from Self Regulatory Organization;
- (ii) manner and the periodicity of furnishing information to SEBI and to its members;

- (iii) arbitration mechanism for resolving disputes between members and/or between members and their constituents;
- (iv) procedure for proceeding against the member committing breach of the governing norms or articles including provisions for suspension or expulsion of members from the Self Regulatory Organization;
- (v) internal control standards including procedure for inspection, auditing, reviewing, monitoring and surveillance of its members by Self Regulatory Organization;
- (vi) code of conduct specifying standards for its members in the conduct of business;
- (vii) procedure for conduct of election of the office bearers and members of the committees;
- (viii) obligation of members to supply such information or explanation and to produce such documents relating to the business as Board of Directors may require;
- (ix) manner of disciplinary action against its members by Self Regulatory Organization;
- (x) contents and format of the annual report;
- (xi) procedure for conduct of the meetings, quorum etc. of Board of Directors;
- (xii) manner of maintaining accounts or records of the Self Regulatory Organization; and,
- (xiii) reporting requirements to SEBI on monthly basis about various aspects of its functioning including policy initiatives, progress in certification, number of members admitted and disciplinary action taken against members, if any.

The governing norms or articles must provide that the contravention of any of the governing norms shall render the member of Self Regulatory Organization concerned liable to one or more of the following punishments, namely:-

- (i) forfeiture of shares;
- (ii) expulsion from membership;
- (iii) suspension from membership for a specified period;
- (iv) any other penalty of a like nature not involving the payment of money.

If SEBI considers it expedient so to do, it may, by order in writing, direct a Self Regulatory Organization to make any governing norms or to amend or revoke any of them within such period as it may specify in this behalf. If a Self Regulatory Organization fails or neglects to comply with such order within the specified period, SEBI can make, amend or revoke the governing norms either in the form specified in the order or with such modifications as it may think fit.

SEBI'S RIGHT TO INSPECT

Regulation 16 of Chapter IV provides that where it appears to SEBI so to do, it may appoint one or more persons as inspecting authority to undertake inspection of the books of accounts, other records and documents of the Self Regulatory Organization.

OBLIGATIONS OF SELF REGULATORY ORGANIZATION

As provided under Regulation 18, it shall be the duty of the Chairman, every director, officer and employee of the Self Regulatory Organization, who is being inspected to produce to the inspecting authority or to any person authorized by him, such books, accounts and other documents in their custody or control and furnish to SEBI the statements and information relating to the activities of Self Regulatory Organization in securities market within such time as SEBI may require. The SRO shall allow the inspecting authority or any person authorized by him to have reasonable access to the premises occupied by the SRO or by any other person on its behalf and also extend reasonable facility for examining any books, records, documents and computer data in the possession

of the SRO or any other person and also provide copies of documents or other materials which, in the opinion of the inspecting authority are relevant.

The inspecting authority in the course of inspection shall be entitled to examine or record statements of the Chairman, Director, any member and employee of the Self Regulatory Organization. It is the duty of the Chairman, every director, officer and employee of the SRO to give to the inspecting authority all assistance in connection with the inspection, which the SRO may reasonably be expected to give.

SUBMISSION OF REPORT AND APPOINTMENT OF AUDITOR

Regulation 19 provides that the inspecting authority shall, as soon as possible, submit an inspection report to SEBI. Under Regulation 20 SEBI can appoint a qualified auditor to inspect the books of account or the affairs of the Self Regulatory Organization.

OBLIGATION OF BOARD OF DIRECTORS

Regulation 22 of Chapter V provides that after receiving the report of an enquiry made under regulation 21, SEBI may take such action as it deems proper and, in particular, may direct Board of Directors of the Self Regulatory Organization to take such disciplinary action against the delinquent member, including expulsion, suspension or any other penalty of a like nature not involving the levy of monetary penalty, as may be specified by it and thereupon, notwithstanding anything to the contrary contained in the articles or governing norms of the Self Regulatory Organization concerned, the Board of Directors of the Self Regulatory Organization shall give effect to the directions of SEBI and shall not in any manner commute, revoke or modify the action taken in pursuance of such directions, without the prior written approval of SEBI.

SEBI may either on its own motion or on representation of the member concerned, modify or withdraw any of its directions issued under sub-regulation (1), if it is satisfied that there are sufficient grounds for doing so.

WITHDRAWAL OF RECOGNITION

Regulation 23 provides that if SEBI is of the opinion that the recognition granted to a Self Regulatory Organization under the provisions of these Regulations should, in the interest of the trade or in the public interest, be withdrawn, it may serve a written notice in Form "C" on Board of Directors of the Self Regulatory Organization calling upon it to show cause as to why the recognition should not be withdrawn for the reasons stated in the notice. Where such notice is issued, SEBI may, after giving an opportunity to Board of Directors of the Self Regulatory Organization to be heard in the matter, withdraw, by passing an order, the recognition granted to the Self Regulatory Organization and thereupon the provisions of regulation 11 would apply as if the application of the Self Regulatory Organization for renewal of recognition has been rejected.

SEBI shall promptly communicate such order to the concerned Self Regulatory Organization. On receipt of the order, the Self Regulatory Organization shall cease to carry on any activity as a Self Regulatory Organization and shall comply with such directions as may be issued by SEBI.

ACTION IN CASE OF VIOLATION

It has been provided under Regulation 24 that if any Self Regulatory Organization, any office bearer or member thereof violates any provisions of the SEBI Act or these regulations, it may be liable for –

- (a) action under Chapter VIA of the Act;
- (b) action under subsection (3) of section 12 of the Act;
- (c) action under subsection (4) of section 11 and section 11B of the Act;
- (d) action under section 24 of the Act;
- (e) such other action permissible under the Act which may be deemed appropriate in the facts and circumstances of the case.

LESSON ROUND UP

- The role of intermediaries makes the market vibrant, and to function smoothly and continuously. Intermediaries possess professional expertise and play a promotional role in organising a perfect match between the supply and demand for capital in the market.
- As per Section 11 of SEBI Act, it is the duty of SEBI to register and regulate the working of stock brokers, sub-brokers, share transfer agents, bankers to an issue, trustees of trust deeds, registrars to an issue, merchant bankers, underwriters, portfolio managers, investment advisors and such other intermediaries who may be associated with securities market in any manner.
- Merchant Bankers are the key intermediaries between the company and issue of capital. The activities of the Merchant Bankers in the Indian capital market are regulated by SEBI (Merchant Bankers) Regulation, 1992.
- Underwriting is compulsory for a public issue. It is necessary for a public company which invites public subscription for its securities to ensure that its issue is fully subscribed.
- Bankers to the issue, as the name suggests, carries out all the activities of ensuring that the funds are collected and transferred to the Escrow accounts.
- A stock broker plays a very important role in the secondary market helping both the seller and the buyer of the securities to enter into a transaction.
- A portfolio manager with professional experience and expertise in the field, studies the market and adjusts the investment mix for his client on a continuing basis to ensure safety of investment and reasonable returns therefrom.
- Every Portfolio manager is required to appoint a Practising Company Secretary or a Practising Chartered Accountant for conducting the internal audit.
- Custodian of securities means any person who carries on or proposes to carry on the business of providing custodial services.
- Investment adviser means any person, who for consideration is engaged in the business of providing investment advice to clients or other group of persons and includes any person who holds out himself as an investment adviser, by whatever name called.
- Section 12 of the Prevention of Money Laundering Act, 2002 lays down certain obligations on an intermediary to be fulfilled.
- All intermediaries are required to appoint a compliance officer who shall be responsible for monitoring the compliance of the Act, rules and regulations, notifications, guidelines, instructions etc. issued by SEBI or Central Government and for redressal of investor grievances. Compliance officer is required to immediately and independently report to SEBI, any non-compliance observed by *him*.
- With a view to bring uniformity in the KYC requirements for the securities markets, SEBI has initiated usage of uniform KYC by all SEBI registered intermediaries.
- SEBI has made it compulsory for all the intermediaries to carry out In Person Verification of their clients.

GLOSSARY

Portfolio

A collection of securities owned by an individual or an institution (such as a mutual fund) that may include stocks, bonds and money market securities.

Investment Profit	Profit which results from the difference between the purchase and selling prices of a security. Trading profit is short term while investment profit is medium or long term.
Netting	A system whereby outstanding financial contracts can be settled at a net figure, i.e. receivables are offset against payables to reduce the credit exposure to a counterparty and to minimize settlement risk.
Institutional Investors	Organisations those invest including insurance companies, depository institutions, pension funds, investment companies and endowment funds.
Financial Planning	It includes analysis of client's current financial situation, identification of their financial goals, and developing and recommending financial strategies to realize such goals.
Inter-operability	Inter-operability means the ability of SEBI to determine whether the KYC documents of the client are in the custody of another KRA.
KYC	KYC means the procedure prescribed by SEBI for identifying and verifying the Proof of Address, Proof of Identity and compliance with rules, regulations, guidelines and circulars issued by SEBI or any other authority for Prevention of Money Laundering from time to time;
Offshore derivative Instruments (ODIs)	These are investment vehicles used by overseas investors for an exposure in Indian equities or equity derivatives. These investors are not register with SEBI.
Self Regulatory Organization	It means an organization of intermediaries which is representing a particular segment of the securities market and which is duly recognised by SEBI under these regulations, but excludes a stock exchange.

SELF TEST QUESTIONS

PART A

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation.)

1. Explain briefly the role and responsibilities of Registrar and Transfer Agent.
2. Explain general obligation and responsibilities of merchant banker.
3. Is underwriter is compulsory for a public issue. If yes, explain the role and responsibilities of underwriter in public issue.
4. Explain the norms for registration as portfolio managers.
5. Discuss conditions of registration of Portfolio Managers and procedure where registration is not granted by SEBI.
6. What are the Obligations of stock-broker in case of inspection by SEBI and liability in case of default made by stock broker.
7. What is the regulation 4 of SEBI (Investment Advisers) Regulations, 2013? *Explain*
8. Short note on additional disclosure by Proxy advisor of SEBI (Research analyst) Regulation, 2014.

PART B

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation.)

1. Discuss the obligation of intermediaries under Prevention Money Laundering Act, 2002.
2. Explain the inspection and disciplinary proceeding which can be initiated by against SEBI registered intermediaries.
3. What are the eligibility criteria to be fulfilled by association for seeking registration under regulation 4 of SEBI(Self-Regulatory Organisation) Regulations, 2004
4. What are actions taken by SEBI, if a Self-Regulatory Organisation violates any provisions of SEBI Act or the regulation make thereunder.

This image shows a blank sheet of white paper designed for writing. At the very top, there is a thick, solid black horizontal bar. Below this bar, the page is filled with evenly spaced, thin grey horizontal lines that run across the entire width of the page, providing a guide for letter height and placement. The margins are consistent throughout.

Lesson 22

Insider Trading – An Overview

LESSON OUTLINE

- Introduction
- Provisions of Companies Act, 2013 relating to Insider Trading
- Powers delegated to SEBI under Companies Act, 2013
- SEBI (Prohibition of Insider Trading) Regulation, 2015
- Important Definitions
- Communication or Procurement of UPSI
- Trading when in possession of UPSI
- Trading plans
- Disclosure of trading by insiders
- Disclosure of interest or holding by certain persons
- Code of fair disclosure and conduct
- Penalty Provisions for violations of the Regulations
- Appeal to Securities Appellate Tribunal
- Role of Company Secretary in Compliance Requirements
- LESSON ROUND UP
- GLOSSARY
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

In simple terms 'insider trading' is buying or selling a security, in breach of a fiduciary duty or other relationship of trust, and confidence, while in possession of material, non-public information about the security. Therefore, preventing such transactions is an important obligation for any capital market regulatory system, because insider trading undermines investor confidence in the fairness and integrity of the securities markets.

A Company Secretary being a professional play an important role in a company to prevent Insider Trading by establishment of policies and procedures in this regard. This lesson will enable the students to have the basic understanding of the Insider trading regulations in India, the disclosures required to be made under the regulations by the company, employee directors, promoters, etc. the duty of compliance officer, Model Code of Conduct, Code of Corporate Disclosure Practices, the Penal provisions for Insider Trading by SEBI and the new provisions of the Insider Trading in the Companies Act, 2013, etc.

INTRODUCTION

The practice of Insider Trading came into existence ever since the very concept of trading of securities of a company became prevalent among the investors worldwide and has now become a formidable challenge for investors all over the world.

The United State of America was the first country to formally enact a legislation to regulate insider trading. Over the years, most of the jurisdictions around the world have recognized the requirement to restrict insider trading in one form or other and accordingly put in place legal restrictions to this effect.

India was not late in recognizing the detrimental impact of insider trading. The history of Insider Trading in India relates back to the 1940's with the formulation of government committees such as the Thomas Committee under the chairmanship of Mr. P.J.Thomas to evaluate restrictions that can be imposed on short swing profit of 1948, which evaluated inter alia, the regulations in the US on short swing profits under Section 16 of the Securities Exchange Act, 1934. Thereafter in India provisions relating to Insider Trading were incorporated in the Companies Act, 1956 under Sections 307 and 308, which required shareholding disclosures by the directors and managers of a company. Due to inadequate provisions of enforcement in the companies Act, 1956, the Sachar Committee in 1979, the Patel Committee in 1986 and the Abid Hussain Committee in 1989 proposed recommendations for a separate statute regulating Insider Trading.

The Patel committee in 1986 in India defined Insider Trading as:

“ Insider trading generally means trading in the shares of a company by the persons who are in the management of the company or are close to them on the basis of undisclosed price sensitive information regarding the working of the company, which they possess but which is not available to others.”

The concept of Insider Trading in India started fermenting in the 80's and 90's and came to be known and observed extensively in the Indian Securities market. As mentioned earlier due to inadequate provisions in the Companies Act, 1956 and rapidly advancing Indian Securities market needed a more comprehensive legislation to regulate the practice of Insider Trading, thus resulting in the formulation of the SEBI (Insider Trading) Regulations in the year 1992, which were amended in the year 2002 after the discrepancies observed in the 1992 regulations in the cases like Hindustan Levers Ltd. vs. SEBI, Rakesh Agarwal vs. SEBI, etc. to remove the lacunae existing in the Regulations of 1992. The amendment in 2002 came to be known as the SEBI (Prohibition of Insider Trading) Regulations, 1992.

Further, the PIT Regulations, 1992 had their challenges in their drafting, interpretation and reach. Besides, the felt need to ensure a clear regulatory policy that is not only easily comprehensible but is also comprehensive led to this Committee being set up under the chairmanship of Justice N. K. Sodhi, Former Chief Justice of the High Courts of Kerala and Karnataka and a Former Presiding Officer of the Securities Appellate Tribunal. The High Level Committee reviewed the SEBI (Prohibition of Insider Trading) Regulations, 1992 submitted its report to SEBI on December 7, 2013.

The Committee made a range of recommendations to the legal framework for prohibition of insider trading in India and has focused on making this area of regulation more predictable, precise and clear by suggesting a combination of principles-based regulations and rules that are backed by principles. The Committee had also suggested that each regulatory provision might be backed by a note on legislative intent.

SEBI has issued and notified the SEBI (Prohibition of Insider Trading) Regulations, 2015 (Regulations) on 15th January, 2015 based on recommendations of Sodhi committee. These Regulations became effective from **120th day of the date of notification i.e. on and from 15th May, 2015, by repealing SEBI (Prohibition of Insider Trading) Regulations 1992.**

The new regulations strengthen the legal and enforcement framework, align Indian regime with international

practices, provide clarity with respect to the definitions and concepts, and facilitate legitimate business transactions.

Now a big step taken forward by introduction of the insider trading provisions in the Companies Act, 2013. As per the Companies Act, 2013 provisions it prohibits directors and key managerial personnel from purchasing call and put options of shares of the company, its holding company and its subsidiary and associate companies as if such person is reasonably expected to have access to price-sensitive information (being information which, if published, is likely to affect the price of the company's securities). Earlier these provisions were contained in regulations framed by SEBI, as the capital market regulator. Now, it has also been informed that SEBI is expected to discuss changes in certain norms for listed firms so as to make them in line with the rules in the new Act.

The definition of price sensitive information has also been included. No person including any director or KMP of a company shall enter into insider trading except any communication required in the ordinary course of business or profession or employment or under any law. While the Companies Act, 1956 was silent on the provisions relating to insider trading, the Companies Act, 2013 on the other hand, lays down provisions relating to prohibition of insider trading with respect to all companies. This is a step towards harmonization between the 2013 Act and the SEBI Act; more specifically for listed companies; Any person who violates the clause will be punished with a cash fine or imprisonment or both.

PROVISIONS RELATING TO INSIDER TRADING IN COMPANIES ACT, 2013

Section 195 of the Companies Act, 2013 deals with the provisions on prohibition on insider trading of securities, which is as under:

Sub-section (1) lays down that no person including any director or key managerial personnel shall enter into insider trading:

However, nothing contained in this sub-section shall apply to any communication required in the ordinary course of business or profession or employment or under any law.

(a) "insider trading" means –

- (i) an act of subscribing, buying, selling, dealing or agreeing to subscribe, buy, sell or deal in any securities by any director or key managerial personnel or any other officer of a company either as principal or agent if such director or key managerial personnel or any other officer of the company is reasonably expected to have access to any non-public price sensitive information in respect of securities of company, or
- (ii) an act of counselling about, procuring or communicating directly or indirectly any non- public price sensitive information to any person;

(b) "price-sensitive information" means any information which relates, directly or indirectly, to a company and which if published is likely to materially affect the price of securities of the company.

Sub-section (2) provides that If any person contravenes the provisions of this section, he shall be punishable with imprisonment for a term which may extend to five years or with fine which shall not be less than five lakh rupees but which may extend to twenty-five crore rupees or three times the amount of profits made out of insider trading, whichever is higher, or with both.

Powers delegated to SEBI under Companies Act 2013

Section 458 (1) states that the Central Government may, by notification, and subject to such conditions, limitations and restrictions as may be specified therein, delegate any of its powers or functions under this Act other than the power to make rules to such authority or officer as may be specified in the notification:

The powers to enforce the provisions contained in section 194 and section 195 relating to forward dealing and

insider trading shall be delegated to the SEBI for listed companies or the companies which intend to get their securities listed and in such case, any officer authorised by the SEBI shall have the power to file a complaint in the court of competent jurisdiction

SEBI (PROHIBITION OF INSIDER TRADING) REGULATIONS, 2015

The SEBI (Prohibition of Insider Trading) Regulation, 2015 comprises of five chapters and two schedules encompassing the various regulations related to insider trading. Chapter I deal mainly with the definitions used in regulation. Chapter II provides for restriction on communication and trading in securities by insiders. Chapter III deals with disclosure of trading by insiders. Chapter IV deals with the code of fair disclosure and conduct to be followed by listed companies and other entities, disclosure requirements. Chapter V deals with miscellaneous matters like sanction for violation, power to remove difficulties, repeal and savings.

Important Definitions

Connected person

“Connected person” means, –

Any person who is or has during the six months prior to the concerned Act been associated with a company, directly or indirectly, in any capacity including by reason of frequent communication with its officers or by being in any contractual, fiduciary or employment relationship or by being a director, officer or an employee of the company or holds any position including a professional or business relationship between himself and the company whether temporary or permanent, that allows such person, directly or indirectly, access to unpublished price sensitive information or is reasonably expected to allow such access.

Insider

“Insider” means any person who is:

- i) a connected person; or
- ii) in possession of or having access to unpublished price sensitive information;

Person deemed to be connected person

“Person is deemed to be a connected person”, if such person –

- (a) an immediate relative of connected persons; or
- (b) a holding company or associate company or subsidiary company; or
- (c) an intermediary as specified in section 12 of the Act or an employee or director thereof; or
- (d) an investment company, trustee company, asset management company or an employee or director thereof; or
- (e) an official of a stock exchange or of clearing house or corporation; or
- (f) a member of board of trustees of a mutual fund or a member of the board of directors of the asset management company of a mutual fund or is an employee thereof; or
- (g) a member of the board of directors or an employee, of a public financial institution as defined in section 2 (72) of the Companies Act, 2013; or
- (h) an official or an employee of a self-regulatory organization recognised or authorized by SEBI; or
- (i) a banker of the company; or
- (j) a concern, firm, trust, Hindu undivided family, company or association of persons wherein a director of a company or his immediate relative or banker of the company, has more than ten per cent of the holding or interest;

Generally available information

“Generally available information” means information that is accessible to the public on a non-discriminatory basis.

Immediate relative

“Immediate relative” means a spouse of a person, and includes parent, sibling, and child of such person or of the spouse, any of whom is either dependent financially on such person, or consults such person in taking decisions relating to trading in securities;

Trading

“Trading” means and includes subscribing, buying, selling, dealing, or agreeing to subscribe, buy, sell, deal in any securities, and “trade” shall be construed accordingly.

Unpublished Price Sensitive Information (UPS)

“Unpublished price sensitive information” means any information, relating to a company or its securities, directly or indirectly, that is not generally available which upon becoming generally available, is likely to materially affect the price of the securities and shall, ordinarily including but not restricted to, information relating to the following–

- (i) Financial results;
- (ii) Dividends;
- (iii) Change in capital structure;
- (iv) Mergers, de-mergers, acquisitions, delisting, disposals and expansion of business and such other transactions;
- (v) Changes in key managerial personnel; and
- (vi) Material events in accordance with the listing agreement

Compliance officer

Compliance Officer means

- any senior officer, designated so and reporting to the board of directors or head of the organization in case board is not there,
- who is financially literate and is capable of appreciating requirements for legal and regulatory compliance under these regulations and
- who shall be responsible for compliance of policies, procedures, maintenance of records, monitoring adherence to the rules for the preservation of unpublished price sensitive information,
- monitoring of trades and the implementation of the codes specified in these regulations under the overall supervision of the board of directors of the listed company or the head of an organization, as the case may be;

COMMUNICATION OR PROCUREMENT OF UNPUBLISHED PRICE SENSITIVE INFORMATION

Regulation 3 provides that any person shall not :

- communicate, provide, or allow access to any unpublished price sensitive information or
- procure from or cause the communication by any insider of unpublished price sensitive information,
- relating to a company or securities listed or proposed to be listed or proposed to be listed

- Except in furtherance of legitimate purposes, performance of duties or discharge of legal obligations.

However, above provisions shall not be applicable to any unpublished price sensitive information that may be communicated, provided, allowed access to or procured, in connection with a transaction that would:–

- entail an obligation to make an open offer under the takeover regulations or
- not attract the obligation to make an open offer under the takeover regulations
- Where the board of directors of the company is of informed opinion that the proposed transaction is in the best interests of the company and
- the information that constitutes unpublished price sensitive information is disseminated to be made generally available at least 2 trading days prior to the proposed transaction being effected in such form as the board of directors may determine.

The board of directors shall require the parties to execute agreements to contract confidentiality and non-disclosure obligations and such parties shall keep information so received confidential, except for the purpose specified above and shall not otherwise trade in securities of the company when in possession of unpublished price sensitive information.

TRADING WHEN IN POSSESSION OF UNPUBLISHED PRICE SENSITIVE INFORMATION

Regulation 4 prescribes that an insider shall not trade in securities, which are listed or proposed to be listed on stock exchange when in possession of unpublished price sensitive information.

However, there are certain exemptions:

- When there is an off-market transfer between promoters
 - who are aware of price sensitive information without being in breach of regulation 3 and
 - both parties had made a conscious and informed trade decision; or
- In the case of non-individual insiders :
 - the individuals who were in possession of such unpublished price sensitive information were different from the individuals taking trading decisions and
 - such decision-making individuals were not in possession of such unpublished price sensitive information when they took the decision to trade; and
 - appropriate and adequate arrangements were in place to ensure that these regulations are not violated and no unpublished price sensitive information was communicated by the individuals possessing the information to the individuals taking trading decisions and
 - there is no evidence of such arrangements having been breached;
- the trades were pursuant to a trading plan set up in accordance with these regulations.

In the case of connected persons, the onus of establishing, that they were not in possession of unpublished price sensitive information, shall be on such connected persons and in other cases, the onus would be on SEBI. SEBI may specify such standards and requirements, from time to time, as it may deem necessary for the purpose of these regulations.

TRADING PLANS

Regulation 5 states that an insider would be required to submit trading plan in advance to the compliance officer for his approval. The compliance officer is also empowered to take additional undertakings from the insiders for

approval of the trading plan. Such trading plan on approval will also be disclosed to the Stock Exchanges, where the securities of the company are listed.

The trading plan shall comply with requirements as follows:

- It shall be submitted for a minimum period of 12 months.
- No overlapping of plan with the existing plan submitted by Insider
- It shall set out either the value of trades to be effected or the number of securities to be traded along with
 - the nature of the trade and
 - the intervals at, or
 - dates on which such trades shall be effected.
- Trading can only commence only after 6 months from public disclosure of plan.
- No trading between 20th day prior to closure of financial period and 2nd trading day after disclosure of financial results.
- Compliance officer to approve the plan.
- The trading plan once approved shall be irrevocable and the insider shall mandatorily have to implement the plan, without being entitled to either deviate from it or to execute any trade in the securities outside the scope of the trading plan.

(Except in few case like where insider is in possession of price sensitive information at the time of formulation of the plan and such information has not become generally available at the time of the commencement of implementation)

- Upon approval of the trading plan, the compliance officer shall notify the plan to the stock exchanges on which the securities are listed.

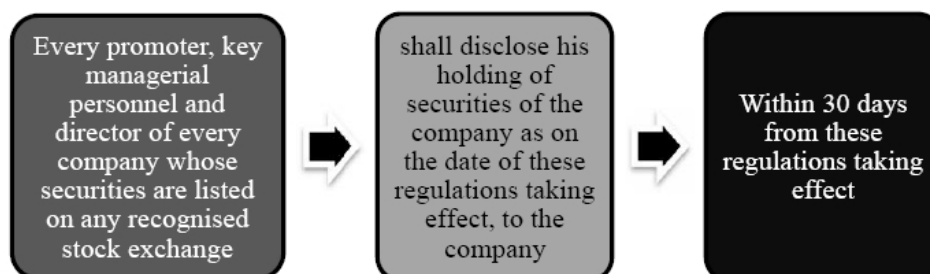
DISCLOSURES OF TRADING BY INSIDERS

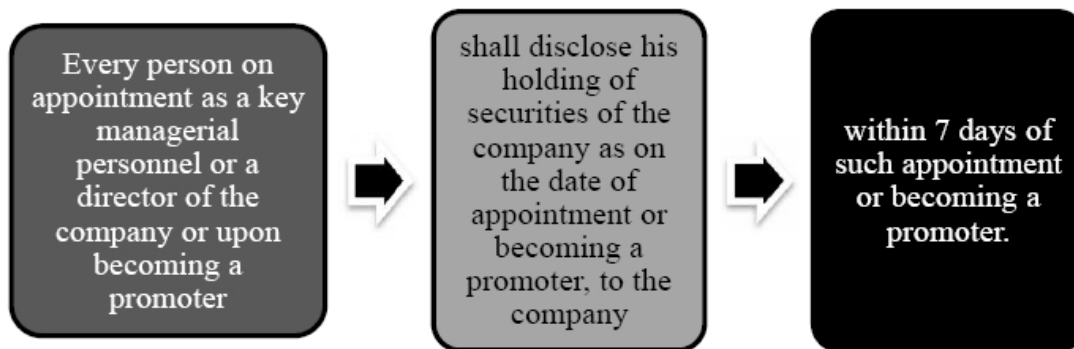
Regulation 6 deals with general provisions of disclosures made :-

- by person shall also include those relating to trading by such person's immediate relatives, and
- by any other person for whom such person takes trading decisions.
- The disclosures of trading in securities shall also include trading in derivatives of securities if permitted under law.
- Such disclosure shall be preserved for 5 years.

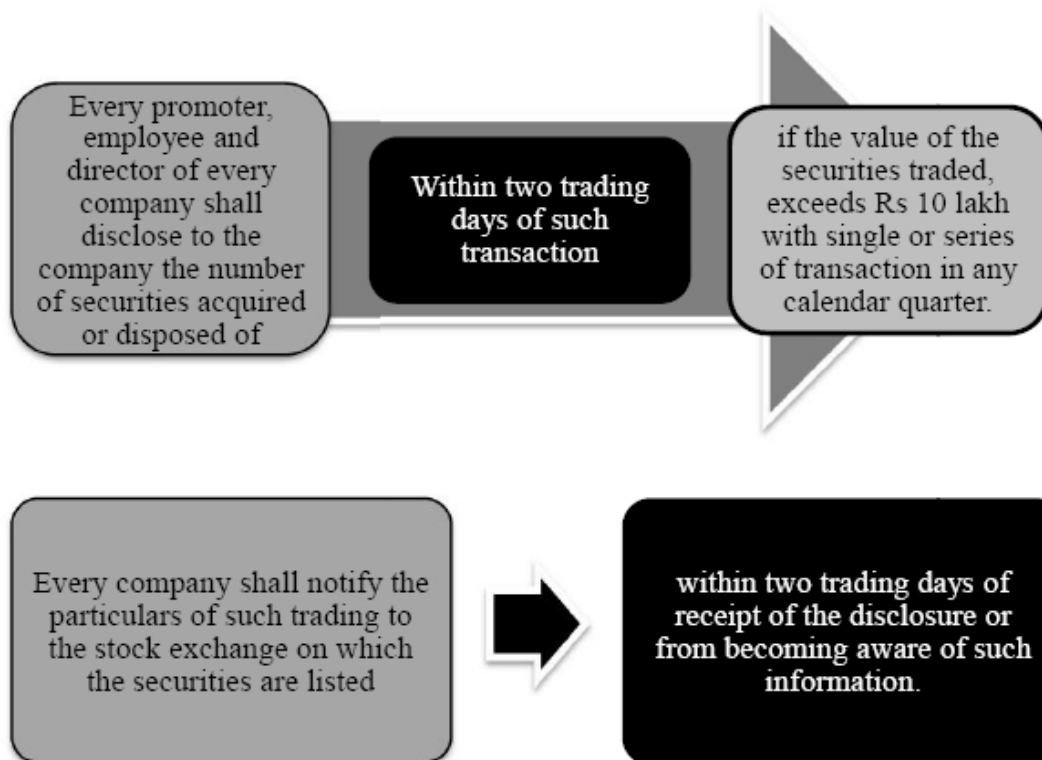
DISCLOSURES OF INTEREST BY CERTAIN PERSONS

INITIAL DISCLOSURE





CONTINUAL DISCLOSURE



Any company whose securities are listed on stock exchange may, at its discretion require any other connected person or class of connected persons to make disclosures of holdings and the company may determine trading in securities of the company in such form and at such frequency as.

CODES OF FAIR DISCLOSURE AND CONDUCT

CODE OF FAIR DISCLOSURE

Where the board of directors of the company, whose securities are listed on a stock exchange, ***shall formulate***

and publish on its official website, a code of practices and procedures for fair disclosure of unpublished price sensitive information which shall follow in order to adhere to each of the principles set out in Schedule A to these regulations, without diluting the provisions of these regulations in any manner.

Every such code of practices and procedures for fair disclosure of unpublished price sensitive information and every amendment thereto shall be promptly intimated to the stock exchanges where the securities are listed.

PRINCIPLES AND PROCEDURES OF FAIR DISCLOSURE

Schedule A of these regulations lays down the following principles of fair disclosure for purposes of Code of Practices and Procedures for Fair Disclosure of Unpublished Price Sensitive Information:-

1. Prompt public disclosure of unpublished price sensitive information that would impact price discovery no sooner than credible and concrete information comes into being in order to make such information generally available.
2. Uniform and universal dissemination of unpublished price sensitive information to avoid selective disclosure.
3. Designation of a senior officer as a chief investor relations officer to deal with dissemination of information and disclosure of unpublished price sensitive information.
4. Prompt dissemination of unpublished price sensitive information that gets disclosed selectively, inadvertently or otherwise to make such information generally available.
5. Appropriate and fair response to queries on news reports and requests for verification of market rumours by regulatory authorities.
6. Ensuring that information shared with analysts and research personnel is not unpublished price sensitive information.
7. Developing best practices to make transcripts or records of proceedings of meetings with analysts and other investor relations conferences on the official website to ensure official confirmation and documentation of disclosures made.
8. Handling of all unpublished price sensitive information on a need-to-know basis.

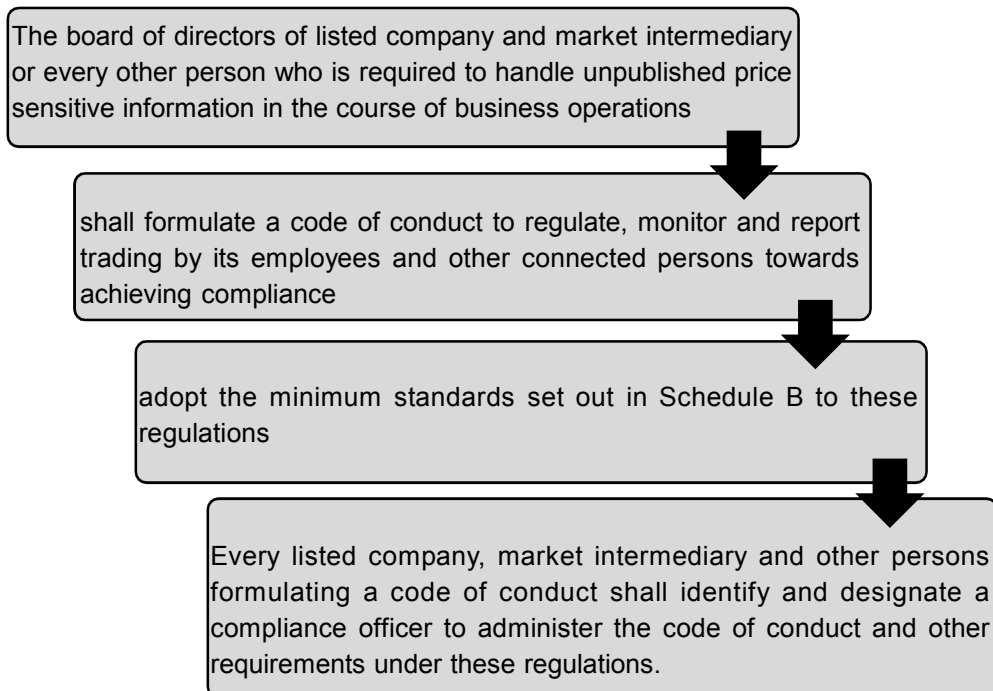
CODE OF CONDUCT

The board of directors of every listed company and market intermediary shall formulate a code of conduct **to regulate, monitor and report** trading by its employees and other connected persons towards achieving compliance with these regulations, adopting the minimum standards as prescribed in this regulations.

Every other person who is required to handle unpublished price sensitive information in the course of business operations shall formulate a code of conduct to regulate, monitor and report trading by employees and other connected persons towards achieving compliance with these regulations, adopting the minimum standards as prescribed in these regulations, without diluting the provisions of these regulations in any manner.

Every listed company, market intermediary and other persons formulating a code of conduct shall identify and designate a compliance officer to administer the code of conduct and other requirements under these regulations.

CODE OF CONDUCT



MINIMUM STANDARDS FOR CODE OF CONDUCT

Schedule B of these regulations lays down the following minimum standards for Code of Conduct to regulate, monitor and report trading by insiders :-

1. The compliance officer shall report to the board of directors and in particular, shall provide reports to the Chairman of the Audit Committee, if any, or to the Chairman of the board of directors at such frequency as may be stipulated by the board of directors.
2. All information shall be handled within the organisation on a need-to-know basis and no unpublished price sensitive information shall be communicated to any person except in furtherance of the insider's legitimate purposes, performance of duties or discharge of his legal obligations.
3. The code of conduct shall contain norms for appropriate Chinese Walls procedures, and processes for permitting any designated person to "cross the wall".
4. Employees and connected persons designated on the basis of their functional role ("**designated persons**") in the organisation shall be governed by an internal code of conduct governing dealing in securities.
5. The board of directors shall in consultation with the compliance officer specify the designated persons to be covered by such code on the basis of their role and function in the organisation. Due regard shall be had to the access that such role and function would provide to unpublished price sensitive information in addition to seniority and professional designation.
6. Designated persons may execute trades subject to compliance with these regulations. Towards this end, a notional trading window shall be used as an instrument of monitoring trading by the designated persons.

7. The trading window shall be closed when the compliance officer determines that a designated person or class of designated persons can reasonably be expected to have possession of unpublished price sensitive information. Such closure shall be imposed in relation to such securities to which such unpublished price sensitive information relates.
8. Designated persons and their immediate relatives shall not trade in securities when the trading window is closed.
9. The timing for re-opening of the trading window shall be determined by the compliance officer taking into account various factors including the unpublished price sensitive information in question becoming generally available and being capable of assimilation by the market, which in any event shall not be earlier than forty-eight hours after the information becomes generally available.
10. The trading window shall also be applicable to any person having contractual or fiduciary relation with the company, such as auditors, accountancy firms, law firms, analysts, consultants etc. assisting, or advising the company.
11. When the trading window is open, trading by designated persons shall be subject to pre-clearance by the compliance officer, if the value of the proposed trades is above such thresholds as the board of directors may stipulate. No designated person shall apply for pre-clearance of any proposed trade if such designated person is in possession of unpublished price sensitive information even if the trading window is not closed.
12. The compliance officer shall confidentially maintain a list of such securities as a “restricted list” which shall be used as the basis for approving or rejecting applications for pre-clearance of trades.
13. Prior to approving any trades, the compliance officer shall be entitled to seek declarations to the effect that the applicant for pre-clearance is not in possession of any unpublished price sensitive information. He shall also have regard to whether any such declaration is reasonably capable of being rendered inaccurate.
14. The code of conduct shall specify any reasonable timeframe, which in any event shall not be more than seven trading days, within which trades that have been pre-cleared have to be executed by the designated person, failing which fresh pre-clearance would be needed for the trades to be executed.
15. The code of conduct shall specify the period, which in any event shall not be less than six months, within which a designated person who is permitted to trade shall not execute a contra trade. The compliance officer may be empowered to grant relaxation from strict application of such restriction for reasons to be recorded in writing provided that such relaxation does not violate these regulations. Should a contra trade be executed, inadvertently or otherwise, in violation of such a restriction, the profits from such trade shall be liable to be disgorged for remittance to SEBI for credit to the Investor Protection and Education Fund administered by SEBI under the Act.
16. The code of conduct shall stipulate such formats as the board of directors deems necessary for making applications for pre-clearance, reporting of trades executed, reporting of decisions not to trade after securing pre-clearance, recording of reasons for such decisions and for reporting level of holdings in securities at such intervals as may be determined as being necessary to monitor compliance with these regulations.
17. The code of conduct shall stipulate the sanctions and disciplinary actions, including wage freeze, suspension etc., that may be imposed, by the persons required to formulate a code of conduct for the contravention of the code of conduct.
18. The code of conduct shall specify that in case it is observed by the persons required to formulate a code of conduct, that there has been a violation of these regulations, they shall inform SEBI promptly.

Flowchart under the SEBI Insider Trading regulations are as follows :

Regulation	Particulars of Compliances	Time frame within which it shall be complied
5	Submission of Trading Plans	Not less than 12 months
7(1)(a)	Initial Disclosure of shareholding by every Promoter, KMP and director to the company	Within 30 days from these regulations taking effect (These Regulations are effective from 120th day of the date of notification i.e. on and from 15th May, 2015)
7(1)(b)	Initial Disclosure of shareholding by every person on appointment as a KMP or a director or upon becoming a promoter to the company	Within 7 days of such appointment or becoming a promoter
7(2)(a)	Continual disclosure of securities acquired or disposed of by promoter, employee and director to the company	Within 2 trading days if the trading value of the securities traded, whether in one transaction or a series of transactions over any calendar quarter, aggregate to a traded value in excess of Rs. 10 lakh.
7(2)(b)	Continual Disclosure of the particulars of trading by the company to stock exchange	Within two trading days of receipt of the disclosure or from becoming aware of such information
8(1) & (2)	Formulation and Publication of a code of practices and procedures for fair disclosure of UPSI or any amendment	On its official website & Promptly intimate to stock exchange

PENALTY PROVISIONS FOR VIOLATIONS OF THE REGULATIONS

If any person violates provisions of these regulations, he shall be liable for appropriate action under Sections 11, 11 B, 11D, Chapter VIA and Section 24 of the SEBI Act.

Regulation 11 & 14 of the Insider regulations empowers the SEBI to issue following directions to the violators without prejudice to its right to initiate criminal prosecution under section 24 or any action under Chapter VIA of the SEBI Act, to protect the interests of investor and in the interests of the securities market and for due compliance with the provisions of the Act, regulation made there under issue any or all of the following order, namely:

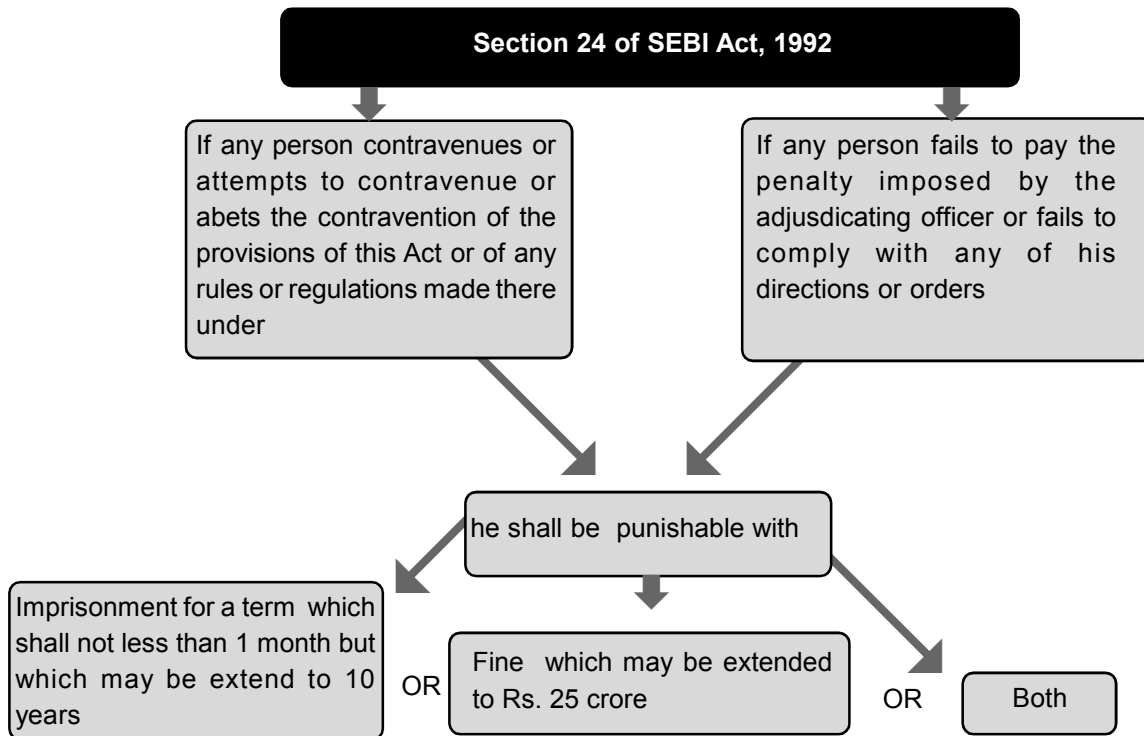
- directing the insider or such person as mentioned in clause (i) of sub-section (2) of section 11 of the Act not to deal in securities in any particular manner;
- prohibiting the insider or such person as mentioned in clause (i) of sub-section (2) of section 11 of the Act from disposing of any of the securities acquired in violation of these regulations;
- restraining the insider to communicate or counsel any person to deal in securities;
- declaring the transaction(s) in securities as null and void;
- directing the person who acquired the securities in violation of these regulations to deliver the securities back to the seller:

However, in case the buyer is not in a position to deliver such securities, the market price prevailing at

the time of issuing of such directions or at the time of transactions whichever is higher, shall be paid to the seller;

- (f) directing the person who has dealt in securities in violation of these regulations to transfer an amount or proceeds equivalent to the cost price or market price of securities, whichever is higher to the investor protection fund of a recognised stock exchange.

PENALTY



Penalty for insider trading under section 15G of SEBI Act

If any Insider who,-

- either on his own behalf or on behalf of any other person, deals in securities of a body corporate listed on any stock exchange on the basis of any unpublished price sensitive information; or
- communicates any unpublished price sensitive information to any person, with or without his request for such information except as required in the ordinary course of business or under any law; or
- counsels, or procures for any other person to deal in any securities of any body corporate on the basis of unpublished price sensitive information,

He shall be liable to a penalty of twenty-five crore rupees or three times the amount of profits made out of insider trading, whichever is higher

Thus, violation of the provisions of the regulations attract huge monetary penalty and may lead to criminal prosecution. However, those aggrieved by an order of SEBI, may prefer an appeal to the Securities Appellate Tribunal within a period of forty-five days of the order.

APPEAL TO SECURITIES APPELLATE TRIBUNAL

Any person aggrieved by an order of SEBI under these regulations can prefer an appeal to the Securities Appellate Tribunal.

ROLE OF COMPANY SECRETARY IN COMPLIANCE REQUIREMENTS

The obligations cast upon the Company Secretary in relation to insider trading regulations can be summarized as under. The Company Secretary shall:

1. Ensure compliance with SEBI (Prohibition of insider Trading) Regulations, 2015 including maintenance of various documents.
2. Frame a code of fair disclosure and conduct in line with the model code specified in the Schedule A of the regulations and get the same approved by the board of directors of the company.
3. Place before SEBI the “minimum standards for Code of Conduct” to regulate, monitor and report trading by insiders as enumerated in the Schedule B of the regulations.
4. Receive initial disclosure from every Promoter, KMP and director or every person on appointment as KMP or director or becoming a Promoter shall disclose its shareholding in the prescribed form within :
 - 30 days from these regulations taking effect or
 - 7 days of such appointment or becoming a promoter
5. Receive from every Promoter, employee and director, continual disclosures of the number of securities acquired or disposed of and changes therein, even if the value of the securities traded, exceeds Rs. 10 lakh with single or series of transaction in any calendar quarter in prescribed form within two trading days of :
 - receipt of the disclosure or
 - from becoming aware of such information
6. Ensure that no trading shall between 20th day prior to closure of financial period and 2nd trading day after disclosure of financial results.
7. Approve the trading plan and after the approval of the trading plan, as compliance officer shall notify the plan to the stock exchanges on which the securities are listed.
8. Maintain records, as a Compliance Officer, of all the declarations given by the directors/designated employees/partners in the appropriate form for a minimum period of three years.
9. Take additional undertakings, as a compliance officer, from the insiders for approval of the trading plan. Such trading plan on approval will also be disclosed to the Stock Exchanges, where the securities of the company are listed.
10. Maintain confidentially list of such securities as a “restricted list” which shall be used as the basis for approving or rejecting applications for pre-clearance of trades.
11. Monitor of trades and the implementation of the code of conduct under the overall supervision of the Board of Directors of the listed company.
12. Frame and then to monitor adherence to the rules for the preservation of “Price sensitive information”.

13. Suggest any improvements required in the policies, procedures, etc. to ensure effective implementation of the code.
14. Assist in addressing any clarifications regarding the SEBI (Prohibition of Insider Trading) Regulations, 2015 and the company's code of conduct.
15. Maintain a list of all information termed as 'price sensitive information'.
16. Maintain a record of names of files containing confidential information deemed to be price sensitive information and persons in charge of the same.
17. Ensure that files containing confidential information are kept secured.
18. Keep records of periods specified as 'close period' and the 'Trading window'.
19. Ensure that the trading restrictions are strictly observed and all directors/officers/designated employees conduct all their dealings in the securities of the company only in a valid trading window and do not deal in the company's securities during the period when the trading window is closed.
20. Receive and maintain records of periodic and annual statement of holdings from directors/officers/designated employees and their dependent family members.
21. Ensure that the "Trading Window" is closed at the time of :
 - a) Declaration of financial results(quarterly, half-yearly and annual)
 - b) Declaration of dividends("interim and final)
 - c) Issue of securities by way of public/right/bonus etc.,
 - d) Any Major expansion plans or execution of new projects.
 - e) Amalgamation, mergers, takeovers and buy-back
 - f) Disposal of whole or substantially whole of the undertaking
 - g) Any change in policies, plans or operations of the company
22. Place before the Chief Executive Officer/Partner or a committee notified by the organization/firm, as a Compliance Officer, on a monthly basis all the details of the dealing in the securities by designated employees/directors/partners of the organization/firm.

LESSON ROUND UP

- To curb insider trading SEBI formulated SEBI (Prohibition of Insider Trading) Regulations, 2015 and which prescribes code of fair disclosure and conduct to be followed by listed companies and entities connected with them.
- The Insider Trading Regulations comprises of five chapter and two schedules encompassing the various regulations relating to Insider Trading.
- Insider means and includes deemed to be a connected person. The definition of deemed to be a connected person is very elaborate.
- The regulations not only seeks to curb dealing in securities, they also seek to curb communicating or counseling about securities by the insiders.
- The regulations provide for initial as well as continual disclosures by members of the company by the directors/ employees/ designated employees/promoter/promoter group at regular interval.

GLOSSARY

Book Closure	The periodic closure of the Register of Members and Transfer Books of the company, to take a record of the shareholders to determine their entitlement to dividends or to bonus or right shares or any other rights pertaining to shares.
Chinese Walls	Artificial barriers to the flow of information set up in large firms to prevent the movement of sensitive information between departments.
Continuous Disclosure	Procedure where certain companies are required to make disclosures on a continuing basis of their business activities by filing documents.
Interim Dividend	A dividend payment made during the course of a company's financial year. Interim dividend, unlike the final dividend, does not have to be agreed in a general meeting.
Punitive	It implies involving or inflicting punishment..

SELF TEST QUESTIONS

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation.)

1. What are the compliances to be made by a company under SEBI (Prohibition of Insider Trading) Regulations, 2015?
2. Describe the obligations cast upon the company under SEBI (Prohibition of Insider Trading) Regulations, 2015.
3. What are the Initial Disclosure Required to be made by a person under SEBI (Insider Trading) Regulations, 2015?
4. What are the Penalty for insider trading under Section 15G of SEBI Act?
5. Briefly explain the duty of Compliance Officer under these regulations.
6. Short note
 - Unpublished price sensitive information (UPSI).
 - Connected Person.

Lesson 23

Takeover Code – An Overview

LESSON OUTLINE

- Introduction
- SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011
- Important Definitions
- Applicability
- Trigger Point for making an open offer by an acquirer
- Open Offer
- Public Announcement
- Offer Price
- Submission of Draft letter of Offer
- Dispatch of Letter of Offer
- Opening of the Offer
- Completion of Requirements
- Restriction on Acquisition
- Provision of Escrow
- Mode of Payment
- Withdrawal of open offer
- Obligations of the Target Company
- Obligations of the Acquirer
- Disclosures
- Exemptions
- LESSON ROUND UP
- GLOSSARY
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

A lot has changed in the corporate world since 1997, the year in which the (SAST) Regulations, 1997 was enacted. In line with the ever changing global scenario this old takeover code was replaced with new SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 ('SAST Regulations'). The main purpose for the takeover code is to prevent hostile takeovers and at the same time, provide some more opportunities of exit to innocent Shareholders who do not wish to be associated with a particular acquirer. The SEBI takeover code will also balance the conflicting objectives and interests of various stakeholders in the context of substantial acquisition of shares in, and takeovers of, listed companies and also regulate and provide for fair and effective competition among acquirers desirous of taking over the same target company.

This lesson provides an overview of the takeover code and after going through this lesson, students will be able to understand the various procedural aspects which an acquirer and target company with respect to takeover.

INTRODUCTION

Takeover code prescribes a systematic framework for acquisition of stake in listed companies. By these laws the regulatory system ensures that the interests of the shareholders of listed companies are not compromised in case of an acquisition or takeover. It also protect the interests of minority shareholders, which is also a fundamental attribute of corporate governance principle.

The takeover code ensures that public shareholders of a listed company are treated fairly and equitably in relation to a substantial acquisition in, or takeover of, a listed company thereby maintaining stability in the securities market. The objective of the takeover regulations is to ensure that the public shareholders of a company are mandatorily offered an exit opportunity from the company at the best possible terms in case of a substantial acquisition in, or change in control of, a listed company.

The earliest attempts at regulating takeovers in India can be traced back to the 1990s with the incorporation of Clause 40 in the earstwhile Listing Agreement. While, the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1994 which were notified in November 1994 made way for regulation of hostile takeovers and competitive offers for the first time; the subsequent regulatory experience from such offers brought out certain inadequacies existing in those Regulations. As a result, the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997 were introduced and notified on February 20, 1997, pursuant to repeal of the 1994 Regulations.

Owing to several factors such as the growth of Mergers & Acquisitions activity in India as the preferred mode of restructuring, the increasing sophistication of takeover market, the decade long regulatory experience and various judicial pronouncements, it was felt necessary to review the Takeover Regulations 1997. Accordingly, SEBI formed a Takeover Regulations Advisory Committee (TRAC) in September 2009 under the Chairmanship of (Late) Shri. C. Achuthan, Former Presiding Officer, Securities Appellate Tribunal (SAT) for this purpose. After extensive public consultation on the report submitted by TRAC, SEBI came out with the SAST Regulations 2011 which were notified on September 23, 2011. The Takeover Regulations, 1997 stand repealed from October 22, 2011, i.e. the date on which SAST Regulations, 2011 come into force.

SAST aims at protecting interest of the investors in securities of a listed company providing amongst others, an opportunity for the public shareholders to exit where there is a substantial acquisition of shares or voting rights or control over a listed company, consolidation of holdings by existing shareholders and related disclosures and penalties for non-compliance etc. SAST requires an acquirer to make an offer to shareholders of the target company on acquiring shares exceeding stipulated thresholds. It also contains provisions relating to open offer size and price, time bound process for making an open offer, exemption from making an open offer, etc.

SEBI (SUBSTANTIAL ACQUISITION OF SHARES AND TAKEOVERS) REGULATIONS, 2011

The SEBI (Substantial Acquisition of Shares and Takeovers) Regulation 2011, comprises of six chapters and one schedules encompassing the various regulations related to Substantial Acquisition of Shares and Takeovers. Chapter I (Regulation 1 – 2) deals mainly with the definitions used in these regulation. Chapter II (Regulation 3-11) provides for substantial acquisition of shares, Voting Rights or Control, threshold limit for open offer. It also contains the exemption available to the company. Chapter III (Regulation 12-23) narrates the open offer process and deals with concept related to open offer. Chapter IV (Regulation 24-27) deals with the other obligations of target company, Acquirer, Manager etc., Chapter V (Regulation 28-31) deals with disclosure requirements of Shareholding and control and limit for making disclosures. Chapter VI (Regulation 32-35) deals with miscellaneous provisions relating to powers of SEBI and its right to issue directions.

What is Takeover?

When an "Acquirer" takes over the control of the "Target Company", it is termed as Takeover. When an acquirer acquires "substantial quantity of shares or voting rights" of the Target Company, it results into substantial acquisition of shares.

IMPORTANT DEFINITIONS

To understand the concept of the takeover code, it would be pertinent to first go through some of the definitions :

Acquirer

"Acquirer" means any person who, directly or indirectly, acquires or agrees to acquire whether by himself, or through, or with persons acting in concert with him, shares or voting rights in, or control over a target company.

Acquisition

"Acquisition" means, directly or indirectly, acquiring or agreeing to acquire shares or voting rights in, or control over, a target company.

Control

"Control" includes the right to appoint majority of the directors or to control the management or policy decisions exercisable by a person or persons acting individually or in concert, directly or indirectly, including by virtue of their shareholding or management rights or shareholders agreements or voting agreements or in any other manner.

However, a director or officer of a target company shall not be considered to be in control over such target company, merely by virtue of holding such position.

Enterprise value

Enterprise value means the value calculated as market capitalization of a company plus debt, minority interest and preferred shares, minus total cash and cash equivalents.

Enterprise Value= Market capitalization+ Debt+ Minority Interest and Preferred Shares- Total Cash and Cash Equivalents

Frequently traded shares

Frequently traded shares means shares of a target company, in which the traded turnover on any stock exchange during the twelve calendar months preceding the calendar month in which the public announcement is made, is at least ten per cent of the total number of shares of such class of the target company.

However, where the share capital of a particular class of shares of the target company is not identical throughout such period, the weighted average number of total shares of such class of the target company shall represent the total number of shares.

Offer period

"Offer period" means the period between the date of entering into an agreement, formal or informal, to acquire shares, voting rights in, or control over a target company requiring a public announcement, or the date of the public announcement, as the case may be, and the date on which the payment of consideration to shareholders who have accepted the open offer is made, or the date on which open offer is withdrawn, as the case may be.

Persons Acting in Concert

"Persons acting in concert" means, –

- (1) persons who, with a common objective or purpose of acquisition of shares or voting rights in, or exercising control over a target company, pursuant to an agreement or understanding, formal or informal, directly

or indirectly co-operate for acquisition of shares or voting rights in, or exercise of control over the target company.

- (2) Without prejudice to the generality of the foregoing, the persons falling within the following categories shall be deemed to be persons acting in concert with other persons within the same category, unless the contrary is established, –
- (i) a company, its holding company, subsidiary company and any company under the same management or control;
 - (ii) a company, its directors, and any person entrusted with the management of the company;
 - (iii) directors of companies referred to in item (i) and (ii) of this sub-clause and associates of such directors;
 - (iv) promoters and members of the promoter group;
 - (v) immediate relatives;
 - (vi) a mutual fund, its sponsor, trustees, trustee company, and asset management company;
 - (vii) a collective investment scheme and its collective investment management company, trustees and trustee company;
 - (viii) a venture capital fund and its sponsor, trustees, trustee company and asset management company;
 - (ix) an alternate investment fund and its sponsor, trustees, trustee company and manager;
 - (x) a merchant banker and its client, who is an acquirer;
 - (xi) a portfolio manager and its client, who is an acquirer;
 - (xii) banks, financial advisors and stock brokers of the acquirer, or of any company which is a holding company or subsidiary of the acquirer, and where the acquirer is an individual, of the immediate relative of such individual.

However, this sub-clause shall not apply to a bank whose sole role is that of providing normal commercial banking services or activities in relation to an open offer under these regulations;

- (xiii) an investment company or fund and any person who has an interest in such investment company or fund as a shareholder or unitholder having not less than 10 per cent of the paid-up capital of the investment company or unit capital of the fund, and any other investment company or fund in which such person or his associate holds not less than 10 per cent of the paid-up capital of that investment company or unit capital of that fund.

However, nothing contained in this sub-clause shall apply to holding of units of mutual funds registered with SEBI.

Target company

Target Company means a company and includes a body corporate or corporation established under a Central legislation, State legislation or Provincial legislation for the time being in force, whose shares are listed on a stock exchange.

Tendering period

Tendering period means the period within which shareholders may tender their shares in acceptance of an open offer to acquire shares made under these regulations.

"Volume weighted average market price"

Volume weighted average market price means the product of the number of equity shares traded on a stock exchange and the price of each equity share divided by the total number of equity shares traded on the stock exchange.

Number of shares traded on the Stock Exchange on a particular day: X, Market Price: Y

Volume Weighted Average Market Price =	$\frac{X1*Y1+X2*Y2+X3*Y3.....}{X1+X2+X3.....}$
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"Weighted average number of total shares"

Weighted average number of total shares means the number of shares at the beginning of a period, adjusted for shares cancelled, bought back or issued during the aforesaid period, multiplied by a time-weighting factor.

"Wilful Defaulter"

Any person who is categorized as a wilful defaulter by any bank or financial institution or consortium thereof, in accordance with the guidelines on wilful defaulters issued by the RBI and includes any person whose director, promoter or principal officer is categorized as such.

"Volume weighted average price"

Volume weighted average price means the product of the number of equity shares bought and price of each such equity share divided by the total number of equity shares bought.

Number of shares bought on a particular day: A, Market Price: B

Volume weighted Average Price =	$\frac{A1*B1+A2*B2+A3*B3.....}{A1+A2+A3.....}$
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APPLICABILITY

These regulations shall apply to direct and indirect acquisition of shares or voting rights, in or control over target company. However, these regulations shall not apply to direct and indirect acquisition of shares or voting rights in, or control over a company listed without making a public issue in the Institutional trading platform of a recognized stock exchange.

TRIGGER POINT FOR MAKING AN OPEN OFFER BY AN ACQUIRER

25% shares or voting rights

An acquirer, along with Persons acting in concert(PAC) , if any, who intends to acquire shares which along with his existing shareholding would entitle him to exercise 25% or more voting rights, can acquire such additional shares only after making a Public Announcement (PA) to acquire minimum twenty six percent shares of the Target Company from the shareholders through an Open Offer.

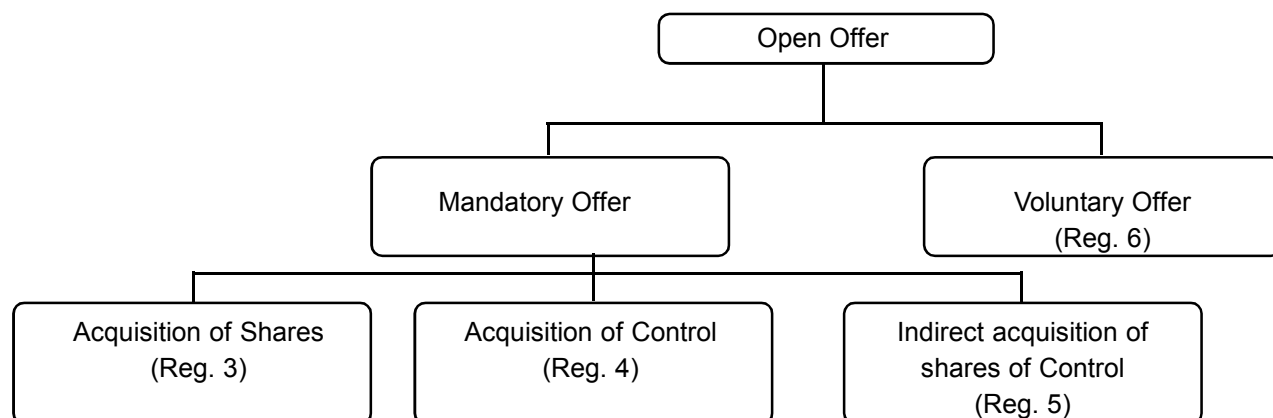
Creeping acquisition limit

An acquirer who holds 25% or more but less than maximum permissible non-public shareholding of the Target Company, can acquire such additional shares as would entitle him to exercise more than 5% of the voting rights in any financial year ending March 31 only after making a Public Announcement to acquire minimum twenty six percent shares of Target Company from the shareholders through an Open Offer.

Name	Per Holding	Creeping Acquisition	Post Holding	Applicability of SEBI Takeover Regulation, 2011
A	23%	3%	26%	Open Offer Obligations
B	7%	2%	9%	–

OPEN OFFER

SEBI Takeover Regulations, 2011 provides certain trigger events wherein the Acquirer is required to give Open Offer to the shareholders of the Target Company to provide them exit opportunity.



I. MANDATORY OPEN OFFER

SEBI Takeover Regulations, 2011 provides a threshold for mandatory Open Offer. The regulations provide that whenever an acquirer acquires the shares in excess of the threshold as prescribed under regulation 3 and 4 of SEBI Takeover Regulations, 2011, then the acquirer is required to make a public announcement of offer to the shareholders of the Target Company.

Regulation 3 of the SEBI Takeover Regulations, 2011 provides that the Acquirer to give an open offer to the shareholders of Target Company on the acquisition of shares or voting rights entitling the Acquirer along with the persons acting in concert with him to exercise 25% or more voting rights in the Target Company.

Further any Acquirer who holds shares between 25%-75%, together with PACs can acquire further 5% shares as creeping acquisition without giving an Open Offer to the shareholders of the Target Company upto a maximum of 75%. The quantum of acquisition of additional voting rights shall be calculated after considering the following:

(a) No Netting off allowed:

For the purpose of determining the quantum of acquisition of additional voting rights, the gross acquisitions without considering the disposal of shares or dilution of voting rights owing to fresh issue of shares by the target company shall be taken into account.

(b) Incremental voting rights in case of fresh issue

In the case of acquisition of shares by way of issue of new shares by the target company, the difference between the pre-allotment and the post-allotment percentage voting rights shall be regarded as the quantum of additional acquisition. [Regulation 3(2)]

The Individual Acquirer Shareholding shall also be considered for determining the Open Offer Trigger Points apart from consolidated shareholding of Acquirer and Persons Acting in Concert. [Regulation 3(3)]

Nothing contained in this regulation shall apply to acquisition of shares or voting rights of a company by the promoters or shareholders in control, in terms of the provisions of VI-A of SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009 [Regulation 3(4)].

Regulation 4 of the SEBI Takeover Regulations, 2011 specifies that if any acquirer including person acting in concert acquires control over the Target Company irrespective of the fact whether there has been any acquisition of shares or not, then he has to give public announcement to acquire shares from shareholders of the Target Company. [Regulation 4]

DELISTING OFFER

Regulation 5A deals with delisting in case of certain cases arising out of open offer which is discussed below:

1. In the event the acquirer makes a public announcement of an open offer for acquiring shares of a target company in terms of regulations 3, 4 or 5, he may delist the company in accordance with provisions of the SEBI (Delisting of Equity Shares) Regulations, 2009 but the acquirer shall have declared upfront his intention to so delist at the time of making the detailed public statement.
2. Where an offer made is not successful-
 - (i) On account of non-receipt of prior approval of shareholders in terms of regulation 8(1)(b) of SEBI (Delisting of Equity Shares) Regulations, 2009; or
 - (ii) in terms of regulation 17 of SEBI (Delisting of Equity Shares) Regulations, 2009; or
 - (iii) on account of the acquirer rejecting the discovered price determined by the book building process in terms of regulation 16(1) of SEBI (Delisting of Equity Shares) Regulations, 2009,

The acquirer shall make an announcement within 2 working days in respect of such failure in all the newspapers in which the detailed public statement was made and shall comply with all applicable provisions of these regulations.

3. In the event of the failure of the delisting offer the acquirer, through the manager to the open offer, shall within five working days from the date of the announcement file with SEBI, a draft of the letter of offer and shall comply with all other applicable provisions of these regulations.

However, the offer price shall stand enhanced by an amount equal to a sum determined at the rate of ten per cent per annum for the period between the scheduled date of payment of consideration to the shareholders and the actual date of payment of consideration to the shareholders.

Note: Scheduled date shall be the date on which the payment of consideration ought to have been made to the shareholders in terms of the timelines in these regulations.

4. Where a competing offer is made -
 - (a) the acquirer shall not be entitled to delist the company;
 - (b) the acquirer shall not be liable to pay interest to the shareholders on account of delay due to competing offer;
 - (c) the acquirer shall comply with all the applicable provisions of these regulations and make an announcement in this regard, within two working days from the date of public announcement made, in all the newspapers in which the detailed public statement was made.
5. Shareholders who have tendered shares in acceptance of the offer, shall be entitled to withdraw such shares tendered, within 10 working days from the date of the announcement.
6. Shareholders who have not tendered their shares in acceptance of the offer shall be entitled to tender their shares in acceptance of the offer made under these regulations.

II. VOLUNTARY OPEN OFFER

Voluntary Open Offer means the Open Offer given by the Acquirer voluntarily without triggering the mandatory Open Offer obligations as envisaged under the regulations. Voluntary Offers are an important means for substantial shareholders to consolidate their stake and therefore recognized the need to introduce a specific framework for such Open Offers.

Regulation 6 of the Takeover Regulations provides the threshold and conditions for making the Voluntary Open Offer which are detailed below:

- **Eligibility-Prior holding of at least 25% shares**

To be eligible for making a Voluntary Open Offer, the regulations mandates the prior holding of atleast 25% stake in the Target Company by the Acquirer along with the PACs.

- **Shareholding of the Acquirer and PACs post completion of Open Offer**

Post completion of the Open Offer, the shareholding of the Acquirer along with PACs shall not exceed the maximum permissible non-public shareholding.

- **Acquisition of shares prior to the Voluntary Open Offer**

The Acquirer shall become ineligible to make a Voluntary Open Offer if during the preceding 52 weeks, the Acquirer or PACs with him has acquired shares of the Target Company without attracting the obligation to make a Public Announcement of an Open Offer. This condition is given because the Voluntary Open Offer is permitted as an exception to the general rule on the offer size, thus the ability to voluntarily make an Open Offer should not be available if in the proximate past, any of such persons have made acquisitions within the creeping acquisition limits permitted under the Regulations.

- **Prohibition on the acquisition of shares during the Offer Period**

SEBI Takeover Regulations, 2011 prohibits the acquirer who has made a Voluntary Open Offer from further acquiring the shares during the Offer Period otherwise than under the Open Offer.

- **Restriction of the acquisition of shares post completion of Voluntary Open Offer**

An acquirer and PACs who have made a Voluntary Open Offer shall not be entitled to further acquire shares for a period of 6 months after completion of the Open Offer except pursuant:

- (a) To another Voluntary Open Offer.
- (b) To Competing Open Offer to the Open Offer made by any other person for acquiring shares of the Target Company.

- **Offer size**

The Voluntary Open Offer shall be made for the acquisition of at least ten per cent (10%) of the voting rights in the Target Company and shall not exceed such number of shares as would result in the post-acquisition holding of the acquirer and PACs with him exceeding the maximum permissible non-public shareholding applicable to such Target Company.

According to Regulation 6A, any person who is a wilful defaulter shall not make a public announcement of an open offer for acquiring shares or enter into any transaction that would attract the obligation to make a public announcement of an open offer for acquiring shares.

This regulation shall not prohibit the wilful defaulter from making a competing offer in accordance with these regulation upon any other person making an open offer for acquiring shares of the target company.

CONDITIONAL OFFER

An offer in which the acquirer has stipulated a minimum level of acceptance is known as a conditional offer.

Minimum level of acceptance implies minimum number of shares which the acquirer desires under the said conditional offer. If the number of shares validly tendered in the conditional offer, are less than the minimum level of acceptance stipulated by the acquirer, then the acquirer is not bound to accept any shares under the offer.

In a conditional offer, if the minimum level of acceptance is not reached, the acquirer shall not acquire any shares in the target company under the open offer or the Share Purchase Agreement which has triggered the open offer.

PUBLIC ANNOUNCEMENT

SEBI (SAST) Regulation, 2011 provides that whenever acquirer acquires the shares or voting rights of the Target Company in excess of the limits prescribed under Regulations 3 and 4, Acquirer is required to give a Public Announcement of an Open Offer to the shareholder of the Target Company. During the process of making

the Public Announcement of an Open Offer, the Acquirer is required to give Public Announcement and publish Detailed Public Statement. The regulations have prescribed the separate timeline for Public Announcement as well as for Detailed Public Statement.

I. Public Announcement

II. Detailed Public Statement

Timing of Public Announcement

The Public Announcement shall be sent to all the stock exchanges on which the shares of the target company are listed. Further, a copy of the same shall also be sent to SEBI and to the target company at its registered office within one working day of the date of the public announcement. The time within which the Public Announcement is required to be made to the Stock Exchanges under different circumstances is tabulated below:

<i>Applicable Regulation</i>	<i>Particulars</i>	<i>Time of making Public Announcement to Stock Exchange</i>
13(1)	Agreement to Acquire Shares or Voting Rights or Control Over The Target Company	On the same day of entering into agreement to acquire share, voting rights or control over the Target Company.
13(c)(a)	Market Purchase of shares	Prior to the placement of purchase order with the stock broker.
13(a)(b)	Acquisition pursuant to conversion of Convertible Securities without a fixed date of conversion or upon conversion of depository receipts for the underlying shares	On the same day when the option to convert such securities into shares is exercised.
13(2)(c)	Acquiring shares or voting rights or control pursuant to conversion of Convertible Securities with a fixed date of conversion	On the second working day preceding the scheduled date of conversion of such securities into shares.
13(2)(d)	In case of disinvestment	On the date of execution of agreement for acquisition of shares or voting rights or control over the Target Company.
13(2)(e)	In case of Indirect Acquisition where the parameters mentioned in Regulation 5(2) are not met	Within four working days of the following dates, whichever is earlier: a. When the primary acquisition is contracted; and b. Date on which the intention or decision to make the primary' acquisition is announced in the public domain.
13(2) (f)	In case of Indirect Acquisition where the parameters mentioned in Regulation 5(2) are met	On the same day of the following dates, whichever is earlier: a. When the primary acquisition is contracted; and b. Date on which the intention or decision to make the primary' acquisition is announced in the public domain.
13(2)(g)	Acquisition of shares, voting rights or control over the Target Company pursuant to Preferential Issue	On the date on which the Board of directors of the target company authorises such preferential issue .

13(2)(h)	Increase in voting rights pursuant to a buy-back not qualifying for exemption under Regulation 10	Not later than 90th day from the date of closure of buy-back offer by the target company.
13(2)(i)	Acquisition of shares, voting rights or control over the Target Company where the such acquisition is beyond the control of acquirer	Not later than two working days from the date of receipt of such intimation.
13(2A)	Acquisition of shares, voting rights in or control over the Target Company through a combination (i) all agreement and any one or more modes of acquisition retrieved to in regulation 13(2), or (ii) any one or more modes of acquisition retinal in clause (a) to (i) of regulation 13(2) or	On the date of first acquisition, provided the acquirer in the public announcement the details of proposed subsequent acquisition.
13(3)	Voluntary Offer	On the same day when the Acquirer decides to make Voluntary Offer

Timing of Detailed Public Statement

In terms of Regulation 13(4) of SEBI (SAST) Regulations, 2011, a Detailed Public Statement shall be published by the acquirer through the Manager to the Open Offer within maximum 5 working days from the date of Public Announcement.

However, in case of Indirect Acquisition where none of condition specified in Regulation 5(2) are satisfied, the Detailed Public Statement shall be published not later than five working days of the completion of the primary acquisition of shares or voting rights in or control over the company or entity holding shares or voting rights in, or control over the target company.

Publication of Public Announcement and Detailed Public Statement

Regulation 14 of SEBI (SAST) Regulation, 2011 provides the requirements relating to publication of Public Announcement and Detailed Public Statement which are tabulated below:

Regulation	Particulars	Time	To whom
14(1)	Public Announcement	On the same day	All the stock exchanges on which the shares of the target company are listed. The stock exchanges shall forthwith disseminate such information to the public.
14(2)	Public Announcement	One working day of the date of the public announcement	Board and to the target company at its registered office
14(3)	Detailed Public Statement	5 working days from the date of Public Announcement.	Publication in the following newspaper: (a) One Hindi national language daily with wide circulation (b) One English national language daily with wide circulation (c) One regional national language daily with wide circulation language at a place where registered office of the company is situated. (d) One regional language daily with wide circulation at the place of the stock exchange where the maximum volume of trading in the shares of the target company is recorded during the sixty trading days preceding the date of the public announcement.

14(4)	Detailed Public Statement		<p>A copy of Detailed Public Statement shall be sent to followings:</p> <p>(a) SEBI</p> <p>(b) All the stock exchanges in which the shares of the target company are listed</p> <p>(c) The target company at its registered office</p>
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After the publication of Detailed Public Statement, the acquirer is further required to file with SEBI a Draft of Letter of Offer within five working days from the date of Detailed Public Statement containing such information as may be specified along with non refundable fees as prescribed by way of banker's cheque or demand draft payable in Mumbai in favor of SEBI.

Offer price

Offer price is the price at which the acquirer announces to acquire shares from the public shareholders under the open offer. The offer price shall not be less than the price as calculated under regulation 8 of the SAST Regulations, 2011 for frequently or infrequently traded shares.

If the target company's shares are frequently traded then the open offer price for acquisition of shares under the minimum open offer shall be highest of the following :

Highest negotiated price per share under the share purchase agreement ("SPA") triggering the offer;

- Volume weighted average price of shares acquired by the acquirer during 52 weeks preceding the public announcement ("PA"),
- Highest price paid for any acquisition by the acquirer during 26 weeks immediately preceding the PA;
- Volume weighted average market price for sixty trading days preceding the PA.

If the target company's shares are infrequently traded then the open offer price for acquisition of shares under the minimum open offer shall be highest of the following:

- Highest negotiated price per share under the share purchase agreement ("SPA") triggering the offer;
- Volume weighted average price of shares acquired by the acquirer during 52 weeks preceding the public announcement ("PA");
- Highest price paid for any acquisition by the acquirer during 26 weeks immediately preceding the PA;
- The price determined by the acquirer and the manager to the open offer after taking into account valuation parameters including book value, comparable trading multiples, and such other parameters that are customary for valuation of shares of such companies.

It may be noted that the SEBI may at the expense of the acquirer, require valuation of shares by an independent merchant banker other than the manager to the offer or any independent chartered accountant in practice having a minimum experience of 10 years.

The shares of the target company will be deemed to be frequently traded if the traded turnover on any stock exchange during the 12 calendar months preceding the calendar month, in which the PA is made, is at least 10% of the total number of shares of the target company. If the said turnover is less than 10%, it will be deemed to be infrequently traded.

SUBMISSION OF DRAFT LETTER OF OFFER

The Acquirer shall submit a draft letter of offer to SEBI within 5 working days from the date of detailed public announcement along with a non-refundable fee as applicable. [Regulation 16(1)]

Simultaneously, a copy of the draft letter of offer shall be send to the Target Company at its registered office and to all the Stock Exchanges where the shares of the Company are listed. [Regulation 18(1)]

DISPATCH OF LETTER OF OFFER [REGULATION 18(2)]

The Acquirer shall ensure that the letter of offer is dispatched to the shareholders whose names appear on the register of members of the Target Company as of the identified date, and to the custodian of shares underlying depository receipts, if any, of the Company, within maximum 7 working days from the date of receipt of communication of comments from SEBI or where no comments are offered by SEBI, within 7 working days from the expiry 15 working days from the date of receipt of draft letter of offer by SEBI.

However, it is provided that where a shareholder holding less than 5% of the voting rights of the Target Company is resident outside India and local laws or regulations of such jurisdiction may expose the acquirer or the target company to material risk of civil, regulatory or criminal liabilities in the event, then the letter of offer in its final form were to be sent without material amendments or modifications into such jurisdiction, then the acquirer may refrain from dispatch of the letter of offer into such jurisdiction.

OPENING OF THE OFFER [REGULATION 18(8)]

The tendering period shall start within maximum 12 working days from date of receipt of comments from SEBI and shall remain open for 10 working days.

COMPLETION OF REQUIREMENTS [REGULATION 18(10)]

Within 10 working days from the last date of the tendering period, the acquirer shall complete all requirements as prescribed under these regulations and other applicable law relating to the Open Offer including payment of consideration to the shareholders who have accepted the open offer.

RESTRICTION ON ACQUISITION [REGULATION 8(10)]

If the acquirer or persons acting in concert with him acquires shares of the target company during the period of 26 weeks after the tendering period at a price higher than the offer price, then the acquirer shall pay the difference between the highest acquisition price and the offer price, to all the shareholders whose shares were accepted in the open offer, within 60 days from the date of such acquisition. However, such provisions shall not be applicable if the acquisition is made through another open offer, Delisting of shares or open market purchase in the ordinary course on the stock exchange.

PROVISION OF ESCROW

Not later than two working days prior to the date of the detailed public statement of the open offer for acquiring shares, the acquirer shall create an escrow account towards security for performance of his obligations under these regulations, and deposit in escrow account such aggregate amount as per the following scale:

S. No.	Consideration payable under the Open Offer	Escrow Amount
(a)	On the first five hundred crore rupees	An amount equal to twenty-five per cent of the consideration
(b)	On the balance consideration	An additional amount equal to ten per cent of the balance consideration

However, where an open offer is made conditional upon minimum level of acceptance, hundred percent of the consideration payable in respect of minimum level of acceptance or fifty per cent of the consideration payable under the open offer, whichever is higher, shall be deposited in cash in the escrow account.

The escrow account may be in the form of, –

- (a) cash deposited with any scheduled commercial bank;
- (b) bank guarantee issued in favour of the manager to the open offer by any scheduled commercial bank;
or
- (c) deposit of frequently traded and freely transferable equity shares or other freely transferable securities with appropriate margin.

<i>Applicable Regulation</i>	<i>Details</i>	
17(4)	Bank Guarantee or Deposit of Security	Deposit at least 1% of the total consideration payable in cash with schedule commercial bank as part of Escrow Account.
17(5)	Cash deposit	Empower the manager to the open offer to instruct the bank to issue a bankers cheque or demand draft or to make payment of the amounts lying to the credit of the escrow account.
17(6)	Bank Guarantee	The bank guarantee shall be in the favor of manager to the offer and shall be kept valid throughout the offer period and additional 30 days after the payment to the shareholders who have tendered their shares have been made.
17(7)	Securities	Manager to the Open Offer shall be empowered to realize the value of escrow account by way of sale or otherwise. Further in case of any shortfall in the amount in the escrow account such shortfall shall be made good by the Manager.

Release of amount from Escrow Account

The amount lying in escrow account can be released in the following cases only:

1. In case of withdrawal of offer, the entire amount can be released only after certification by the merchant banker.
2. The amount deposited in escrow account is transferred to special bank account opened with the bankers to an issue. However, the amount so transferred shall not exceed 90% of the cash deposit.
3. The balance 10% is released to the acquirer on the expiry of thirty days from the completion of all obligations under the offer.
4. The entire amount to the acquirer on the expiry of thirty days from the completion of all obligations under the offer where the open offer is for exchange of shares or other secured instruments.
5. In the event of forfeiture of amount, the entire amount is distributed in the following manner:
 - One third of the amount to Target Company;
 - One third of the escrow account to the Investor Protection and Education Fund established under SEBI (Investor Protection and Education Fund) Regulations, 2009;
 - Residual one third is to be distributed to the shareholders who have tendered their shares in the offer.

MODE OF PAYMENT

The offer price may be paid, –

- (a) in cash;

- (b) by issue, exchange or transfer of listed shares in the equity share capital of the acquirer or of any person acting in concert;
- (c) by issue, exchange or transfer of listed secured debt instruments issued by the acquirer or any person acting in concert with a rating not inferior to investment grade as rated by a credit rating agency registered with SEBI;
- (d) by issue, exchange or transfer of convertible debt securities entitling the holder thereof to acquire listed shares in the equity share capital of the acquirer or of any person acting in concert; or
- (e) a combination of the mode of payment of consideration stated in clause (a), clause (b), clause (c) and clause (d).

Where any shares have been acquired or agreed to be acquired by the acquirer and persons acting in concert with him during the fifty-two weeks immediately preceding the date of public announcement constitute more than ten per cent of the voting rights in the target company and has been paid for in cash, the open offer shall entail an option to the shareholders to require payment of the offer price in cash, and a shareholder who has not exercised an option in his acceptance shall be deemed to have opted for receiving the offer price in cash. In case of revision in offer price the mode of payment of consideration may be altered subject to the condition that the component of the offer price to be paid in cash prior to such revision is not reduced.

WITHDRAWAL OF OPEN OFFER [Regulation 23]

1. An open offer for acquiring shares once made shall not be withdrawn except under any of the following circumstances, –
 - (a) statutory approvals required for the open offer or for effecting the acquisitions attracting the obligation to make an open offer under these regulations having been finally refused, subject to such requirements for approval having been specifically disclosed in the detailed public statement and the letter of offer;
 - (b) the acquirer, being a natural person, has died;
 - (c) any condition stipulated in the agreement for acquisition attracting the obligation to make the open offer is not met for reasons outside the reasonable control of the acquirer, then it should be disclosed in the detailed public statement and the letter of offer; or
 - (d) such circumstances as in the opinion of the SEBI, merit withdrawal.

SEBI shall pass a reasoned order permitting withdrawal and such order shall be listed by SEBI on its official website. However, an acquirer shall not withdraw an open offer pursuant to a public announcement made under clause (g) of sub-regulation (2) of regulation 13, even if the proposed acquisition through the preferential issue is not successful.
2. In the event of withdrawal of the open offer, the acquirer shall through the manager to the open offer, within two working days, –
 - (a) make an announcement in the same newspapers in which the public announcement of the open offer was published, providing the grounds and reasons for withdrawal of the open offer; and
 - (b) simultaneously with the announcement, inform in writing to,—
 - (i) SEBI;
 - (ii) all the stock exchanges on which the shares of the target company are listed, and the stock exchanges shall forthwith disseminate such information to the public; and
 - (iii) the target company at its registered office.

OBLIGATIONS OF THE TARGET COMPANY

Upon a public announcement of an open offer for acquiring shares of a target company being made, the board of directors of such target company shall ensure that during the offer period, the business of the target company is conducted in the ordinary course consistent with past practice.

During the offer period, unless the approval of shareholders of the target company by way of a special resolution by postal ballot is obtained, the board of directors of either the target company or any of its subsidiaries shall not, –

- (a) alienate any material assets whether by way of sale, lease, encumbrance or otherwise or enter into any agreement therefore outside the ordinary course of business;
- (b) effect any material borrowings outside the ordinary course of business;
- (c) issue or allot any authorised but unissued securities entitling the holder to voting rights.

However, the target company or its subsidiaries may, –

- (i) issue or allot shares upon conversion of convertible securities issued prior to the public announcement of the open offer, in accordance with pre-determined terms of such conversion;
- (ii) issue or allot shares pursuant to any public issue in respect of which the red herring prospectus has been filed with the Registrar of Companies prior to the public announcement of the open offer; or
- (iii) issue or allot shares pursuant to any rights issue in respect of which the record date has been announced prior to the public announcement of the open offer;
- (d) implement any buy-back of shares or effect any other change to the capital structure of the target company;
- (e) enter into, amend or terminate any material contracts to which the target company or any of its subsidiaries is a party, outside the ordinary course of business, whether such contract is with a related party, within the meaning of the term under applicable accounting principles, or with any other person; and
- (f) accelerate any contingent vesting of a right of any person to whom the target company or any of its subsidiaries may have an obligation, whether such obligation is to acquire shares of the target company by way of employee stock options or otherwise.

(3) In any general meeting of a subsidiary of the target company in respect of the matters referred to in sub-regulation (2), the target company and its subsidiaries, if any, shall vote in a manner consistent with the special resolution passed by the shareholders of the target company.

(4) The target company shall be prohibited from fixing any record date for a corporate action on or after the third working day prior to the commencement of the tendering period and until the expiry of the tendering period.

(5) The target company shall furnish to the acquirer within two working days from the identified date, a list of shareholders as per the register of members of the target company containing names, addresses, shareholding and folio number, in electronic form, wherever available, and a list of persons whose applications, if any, for registration of transfer of shares are pending with the target company:

However, the acquirer shall reimburse reasonable costs payable by the target company to external agencies in order to furnish such information.

(6) Upon receipt of the detailed public statement, the board of directors of the target company shall constitute a committee of independent directors to provide reasoned recommendations on such open offer, and the target company shall publish such recommendations.

However, such committee shall be entitled to seek external professional advice at the expense of the target company.

(7) The committee of independent directors shall provide its written reasoned recommendations on the open offer to the shareholders of the target company and such recommendations shall be published in such form as may be specified, at least two working days before the commencement of the tendering period, in the same newspapers where the public announcement of the open offer was published, and simultaneously, a copy of the same shall be sent to, –

- (i) SEBI;
- (ii) all the stock exchanges; and
- (iii) to the manager to the open offer, and where there are competing offers, to the manager to the open offer for every competing offer.

(8) The board of directors of the target company shall facilitate the acquirer in verification of shares tendered in acceptance of the open offer.

(9) The board of directors of the target company shall make available to all acquirers making competing offers, any information and co-operation provided to any acquirer who has made a competing offer.

(10) Upon fulfillment by the acquirer, of the conditions required under these regulations, the board of directors of the target company shall without any delay register the transfer of shares acquired by the acquirer in physical form, whether under the agreement or from open market purchases, or pursuant to the open offer.

OBLIGATIONS OF THE ACQUIRER

(1) Prior to making the public announcement of an open offer for acquiring shares under these regulations, the acquirer shall ensure that firm financial arrangements have been made for fulfilling the payment obligations under the open offer and that the acquirer is able to implement the open offer, subject to any statutory approvals for the open offer that may be necessary.

(2) In the event the acquirer has not declared an intention in the detailed public statement and the letter of offer to alienate any material assets of the target company or of any of its subsidiaries whether by way of sale, lease, encumbrance or otherwise outside the ordinary course of business, the acquirer, where he has acquired control over the target company, shall be debarred from causing such alienation for a period of two years after the offer period.

However, in the event the target company or any of its subsidiaries is required to so alienate assets despite the intention to alienate not having been expressed by the acquirer, such alienation shall require a special resolution passed by shareholders of the target company, by way of a postal ballot and the notice for such postal ballot shall *inter alia* contain reasons as to why such alienation is necessary.

(3) The acquirer shall ensure that the contents of the public announcement, the detailed public statement, the letter of offer and the post-offer advertisement are true, fair and adequate in all material aspects and not misleading in any material particular, and are based on reliable sources, and state the source wherever necessary.

(4) The acquirer and persons acting in concert with him shall not sell shares of the target company held by them, during the offer period.

(5) The acquirer and persons acting in concert with him shall be jointly and severally responsible for fulfillment of applicable obligations under these regulations.

DISCLOSURES

In SEBI Takeover Regulations, 2011, the obligation to give the disclosures on the acquisition of certain limits is only on the acquirer and not on the Target Company. Further as against the Open Offer obligations where the individual shareholding is also to be considered, the disclosure shall be of the aggregated shareholding and voting rights of the acquirer or promoter of the target company or every person acting in concert with him.

Clause 29(2) even if such change in shareholding or voting rights result in shareholding falling below 5%, if there is change in such holding from last disclosure made

EVENT BASED DISCLOSURES

Regulation	Made	Trigger	Time Period	Made to
Regulation 29(1)	Acquirer	Acquirer + Persons acting in concert (PAC) acquiring 5% or more shares of the target company	2 working days of the receipt of intimation of allotment of shares, or the acquisition of shares or voting rights	SE where the shares are listed and the target company
Regulation 29(2)	Acquirer	The number of shares or voting rights held and change in shareholding or voting rights, even if such change results in shareholding falling below five per cent and such change exceed 2% of total shareholding or voting rights in the target company by the Acquirer + PAC holding 5% or more shares, of the target company or voting rights.		

Note :

- Shares taken by way of encumbrance shall be treated as an “acquisition”.
- Share given upon release of encumbrance shall be treated as a “disposal”
- The requirement as listed above shall not apply to a Scheduled Commercial bank or public financial institution as pledge in connection with a pledge of shares for securing indebtedness in the ordinary course of business.

CONTINUAL DISCLOSURES

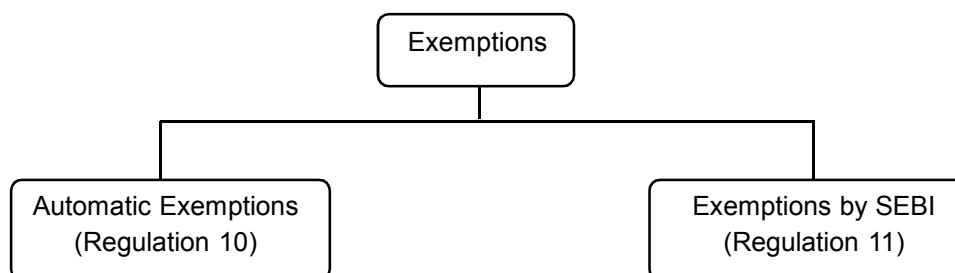
Regulation	Trigger	Time Period	Made to
Regulation 30(1)	Any Person + PAC holding more than 25% shares or voting rights in the target to disclose their aggregate shareholding and voting rights	Within 7 working days from the financial year ending 31st March every year	SE where the shares are listed and target company

DISCLOSURES of Pledged/Encumbered Shares

Regulation	Made	Trigger	Time Period	Made to
Regulation 31(1)	Promoter	Promoter + PAC pledging or creating encumbrance on the shares of the target company	Within 7 working days from the creation, invocation or release of pledge	Stock exchange where the shares are listed and target company
Regulation 31(2)	Acquirer	Invocation or release of the pledge or encumbrance on the shares of the target company		

EXEMPTIONS

While the fundamental objective of the Takeover Code is investor protection, the Takeover Code like the 1997 Code also provides for certain exemptions from the open offer obligation without deviating from its objective.

**Regulation 10 - Automatic Exemptions**

Regulation 10 of the SEBI Takeover Regulations, 2011 provides for automatic exemptions from the applicability of making Open Offer to the shareholders of the Target Company in respect of certain acquisitions subject to the compliance of certain conditions specified therein.

Further, Regulation 11 of SEBI Takeover Regulations, 2011 provides the provisions whereby the acquirer can apply to SEBI for availing the exemption from the Open Offer obligations and the Target Company can apply for relaxation from strict compliance with any procedural requirement relating to Open Offer as provided under Chapter III and IV of these regulations.

Some of the important exemptions provided therein regulation 10 along with their conditions for exemption are detailed below:

The following acquisitions shall be exempt from the obligation to make an open offer under regulation 3 and regulation 4 :

- (1) (a) acquisition pursuant to *inter se* transfer of shares amongst qualifying persons, being, –
 - (i) immediate relatives;
 - (ii) persons named as promoters in the shareholding pattern filed by the target company in terms of the listing agreement or these regulations for not less than three years prior to the proposed acquisition;
 - (iii) a company, its subsidiaries, its holding company, other subsidiaries of such – holding company, persons holding not less than fifty per cent of the equity shares of such company, other companies in which such persons hold not less than fifty per cent of the equity shares, and their subsidiaries subject to control over such qualifying persons being exclusively held by the same persons;

- (iv) persons acting in concert for not less than three years prior to the proposed acquisition, and disclosed as such pursuant to filings under the listing agreement;
- (v) shareholders of a target company who have been persons acting in concert for a period of not less than three years prior to the proposed acquisition and are disclosed as such pursuant to filings under the listing agreement, and any company in which the entire equity share capital is owned by such shareholders in the same proportion as their holdings in the target company without any differential entitlement to exercise voting rights in such company:

However, for purposes of availing of the exemption under this clause, –

- (i) If the shares of the target company are frequently traded, the acquisition price per share shall not be higher by more than twenty-five per cent of the volume-weighted average market price for a period of sixty trading days preceding the date of issuance of notice for the proposed inter se transfer, as traded on the stock exchange where the maximum volume of trading in the shares of the target company are recorded during such period, and if the shares of the target company are infrequently traded, the acquisition price shall not be higher by more than twenty-five percent of the price determined; and
- (ii) the transferor and the transferee shall have complied with applicable disclosure requirements set out in these regulations.

(b) acquisition in the ordinary course of business by, –

- (i) an underwriter registered with SEBI by way of allotment pursuant to an underwriting agreement in terms of the SEBI (ICDR) Regulations, 2009;
- (ii) a stock broker registered with SEBI on behalf of his client in exercise of lien over the shares purchased on behalf of the client under the bye-laws of the stock exchange where such stock broker is a member;
- (iii) a merchant banker registered with SEBI or a nominated investor in the process of market making or subscription to the unsubscribed portion of issue in terms of Chapter XB of SEBI (ICDR) Regulations, 2009;
- (iv) any person acquiring shares pursuant to a scheme of safety net in terms of SEBI (ICDR) Regulations, 2009;
- (v) a merchant banker registered with SEBI acting as a stabilising agent or by the promoter or pre-issue shareholder in terms of SEBI (ICDR) Regulations, 2009;
- (vi) by a registered market-maker of a stock exchange in respect of shares for which he is the market maker during the course of market making;
- (vii) a Scheduled Commercial Bank, acting as an escrow agent; and
- (viii) invocation of pledge by Scheduled Commercial Banks or Public Financial Institutions as a pledgee.

(c) acquisitions at subsequent stages, by an acquirer who has made a public announcement of an open offer for acquiring shares pursuant to an agreement of disinvestment, as contemplated in such agreement: However, (i) both the acquirer and the seller are the same at all the stages of acquisition; and (ii) full disclosures of all the subsequent stages of acquisition, if any, have been made in the public announcement of the open offer and in the letter of offer.

(d) acquisition pursuant to a scheme, –

- (i) made under section 18 of the Sick Industrial Companies (Special Provisions) Act, 1985 or any statutory modification or re-enactment thereto;

- (ii) of arrangement involving the target company as a transferor company or as a transferee company, or reconstruction of the target company, including amalgamation, merger or demerger, pursuant to an order of a court or a tribunal or a competent authority under any law or regulation, Indian or foreign; or
 - (iii) of arrangement not directly involving the target company as a transferor company or as a transferee company, or reconstruction not involving the target company's undertaking, including amalgamation, merger or demerger, pursuant to an order of a court or a tribunal or a competent authority under any law or regulation, Indian or foreign, subject to, –
 - A. the component of cash and cash equivalents in the consideration paid being less than twenty-five per cent of the consideration paid under the scheme; and
 - B. where after implementation of the scheme of arrangement, persons directly or indirectly holding at least thirty-three per cent of the voting rights in the combined entity are the same as the persons who held the entire voting rights before the implementation of the scheme.
 - (da) acquisition pursuant to a resolution plan approved under section 31 of the Insolvency and Bankruptcy Code, 2016.
 - (e) acquisition pursuant to the provisions of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002;
 - (f) acquisition pursuant to the provisions of SEBI (Delisting of Equity Shares) Regulations, 2009;
 - (g) acquisition by way of transmission, succession or inheritance;
 - (h) acquisition of voting rights or preference shares carrying voting rights arising out of the operation of sub-section (2) of section 47 of the Companies Act, 2013.
 - (i) Acquisition of shares by the lenders pursuant to conversion of their debt as part of a debt restructuring scheme implemented in accordance with the guidelines specified by RBI.
- However, the conditions specified under sub-regulation (5) of regulation 70 of the SEBI (ICDR) Regulations, 2009 are complied with.
- (ia) Acquisition of shares by the person(s), by way of allotment by the target company or purchase from the lenders at the time of lenders selling their shareholding or enforcing change in ownership in favour of such person(s), pursuant to a debt restructuring scheme implemented in accordance with the guidelines specified by RBI.

However, in respect of acquisition by persons by way of allotment by the target company, the conditions specified under regulation 70(6) of the SEBI (ICDR) Regulations, 2009 are complied with.

Further that in respect of acquisition by way of purchase of shares from the lenders, the acquisition shall be exempted subject to the compliance with the following conditions:

- (a) the guidelines for determining the purchase price have been specified by the RBI and that the purchase price has been determined in accordance with such guidelines;
- (b) the purchase price shall be certified by two independent qualified valuers, and "Valuer" shall be a person who is registered under section 247 of the Companies Act, 2013 and the relevant Rules framed thereunder.

However, till such date on which section 247 of the Companies Act, 2013 and the relevant Rules come into force, valuer shall mean an independent merchant banker registered with SEBI or an independent chartered accountant in practice having a minimum experience of ten years;

- (c) specified securities shall be locked-in for a period of at least three years from the date of purchase;

- (d) the lock-in of equity shares acquired pursuant to conversion of convertible securities purchased from the lenders shall be reduced to the extent the convertible securities have already been locked-in;
 - (e) a special resolution has been passed by shareholders before the purchase;
 - (f) the issuer shall, in addition to the disclosures required under the Companies Act, 2013 or any other applicable law, disclose the following information pertaining to the proposed acquirer(s) in the explanatory statement to the notice for the general meeting proposed for passing special resolution as stipulated at clause (e) of this sub-regulation:
 - a. the identity including of the natural persons who are the ultimate beneficial owners of the shares proposed to be purchased and/ or who ultimately control the proposed acquirer(s);
 - b. the business model;
 - c. a statement on growth of business over the period of time;
 - d. summary of audited financials of previous three financial years;
 - e. track record in turning around companies, if any;
 - f. the proposed roadmap for effecting turnaround of the issuer.
 - (g) Applicable provisions of the Companies Act, 2013 are complied with.
 - (j) increase in voting rights arising out of the operation of sub-section (1) of section 106 of the Companies Act, 2013 or pursuant to a forfeiture of shares by the target company, undertaken in compliance with the provisions of the Companies Act, 2013 and its articles of association
- (2) The acquisition of shares of a target company, not involving a change of control over such target company, pursuant to a scheme of corporate debt restructuring in terms of the Corporate Debt Restructuring Scheme notified by the Reserve Bank of India vide Circular No. B.P.BC 15/21.04, 114/2001 dated August 23, 2001, or any modification or re-notification thereto provided such scheme has been authorised by shareholders by way of a special resolution passed by postal ballot, shall be exempted from the obligation to make an open offer under regulation 3.
- (3) An increase in voting rights in a target company of any shareholder beyond the limit attracting an obligation to make an open offer under sub-regulation (1) of regulation 3, pursuant to buy-back of shares by the target company shall be exempt from the obligation to make an open offer provided such shareholder reduces his shareholding such that his voting rights fall to below the threshold referred to in sub-regulation (1) of regulation 3 within ninety days from the date of the closure of the said buy back offer.
- (4) The following acquisitions shall be exempt from the obligation to make an open offer under sub-regulation (2) of regulation 3, –
- (a) acquisition of shares by any shareholder of a target company, upto his entitlement, pursuant to a rights issue;
 - (b) acquisition of shares by any shareholder of a target company, beyond his entitlement, pursuant to a rights issue, subject to fulfillment of the following conditions, –
 - (i) the acquirer has not renounced any of his entitlements in such rights issue; and
 - (ii) the price at which the rights issue is made is not higher than the ex-rights price of the shares of the target company, being the sum of, –
 - (A) the volume weighted average market price of the shares of the target company during a period of sixty ending on the day prior to the date of determination of the rights issue price, multiplied

by the number of shares outstanding prior to the rights issue, divided by the total number of shares outstanding after allotment under the rights issue. However, such volume weighted average market price shall be determined on the basis of trading on the stock exchange where the maximum volume of trading in the shares of such target company is recorded during such period; and

(B) the price at which the shares are offered in the rights issue, multiplied by the number of shares so offered in the rights issue divided by the total number of shares outstanding after allotment under the rights issue.

- (c) increase in voting rights in a target company of any shareholder pursuant to buy-back of shares. However,
 - (i) such shareholder has not voted in favour of the resolution authorising the buy-back of securities under section 68 of the Companies Act, 2013;
 - (ii) in the case of a shareholder resolution, voting is by way of postal ballot;
 - (iii) where a resolution of shareholders is not required for the buy-back, such shareholder, in his capacity as a director, or any other interested director has not voted in favour of the resolution of the board of directors of the target company authorising the buy-back of securities under section 68 of the Companies Act, 2013; and
 - (iv) the increase in voting rights does not result in an acquisition of control by such shareholder over the target company. However, where the aforesaid conditions are not met, in the event such shareholder reduces his shareholding such that his voting rights fall below the level at which the obligation to make an open offer would be attracted under sub-regulation (2) of regulation 3, within ninety days from the date of closure of the buy-back offer by the target company, the shareholder shall be exempt from the obligation to make an open offer;
- (d) acquisition of shares in a target company by any person in exchange for shares of another target company tendered pursuant to an open offer for acquiring shares under these regulations;
- (e) acquisition of shares in a target company from state-level financial institutions or their subsidiaries or companies promoted by them, by promoters of the target company pursuant to an agreement between such transferors and such promoter;
- (f) acquisition of shares in a target company from a venture capital fund or foreign venture capital investor registered with SEBI, by promoters of the target company pursuant to an agreement between such venture capital fund or category I Alternative Investment Fund or foreign venture capital investor and such promoters.

(5) In respect of acquisitions under clause (a) of sub-regulation (1), and clauses (e) and (f) of sub-regulation (4), the acquirer shall intimate the stock exchanges where the shares of the target company are listed, the details of the proposed acquisition in such form as may be specified, at least four working days prior to the proposed acquisition, and the stock exchange shall forthwith disseminate such information to the public.

(6) In respect of any acquisition made pursuant to exemption provided for in this regulation, the acquirer shall file a report with the stock exchanges where the shares of the target company are listed, in such form as may be specified not later than four working days from the acquisition, and the stock exchange shall forthwith disseminate such information to the public.

(7) In respect of any acquisition of or increase in voting rights pursuant to exemption provided for in clause (a) of sub-regulation (1), sub-clause (iii) of clause (d) of sub-regulation (1), clause (h) of sub-regulation (1), sub-regulation (2), sub-regulation (3) and clause (c) of sub-regulation (4), clauses (a), (b) and (f) of sub-regulation (4), the acquirer shall, within twenty-one working days of the date of acquisition, submit a report in such form as may be specified along with supporting documents to SEBI giving all details in respect of acquisitions, along with a non-

refundable fee of rupees one lakh fifty thousand by way of direct credit in the bank account through NEFT/RTGS/IMPS or any other mode allowed by RBI or by way of a, banker's cheque or demand draft payable in Mumbai in favour of SEBI.

Regulation 11 – Exemption by SEBI

Regulation 11 provides that on an application being made by the acquirer in writing giving the details of the proposed acquisition and grounds on which the exemption is sought along with duly sworn affidavit, SEBI may grant exemption to the acquirer from the Open Offer obligations subject to the compliance with such conditions as it deems fits. For instance, in case where the exemptions is sought from the Open Offer obligations which has been triggered pursuant to the issue of shares by way preferential allotment, SEBI may require that the approval of shareholders should be obtained by way of postal ballot. Further, along with the application, the acquirer is also required to pay a non refundable fee of ₹ 5,00,000, by way of direct credit in the bank account through NEFT/RTGS/IMPS or any other mode allowed by or by way of banker's cheque or demand draft in payable in favour of Mumbai.

However, it is to be noted that the Acquirer is not exempted from making other compliances related to the disclosure requirements as provided under regulation 29, 30 and 31 of the SEBI Takeover Regulations, 2011.

Regulation	Particulars of Compliances	Time frame within which it shall be complied
	PUBLIC ANNOUNCEMENT	
13(1)	Agreement to acquire shares or voting rights or control over the Target Company	On the same day of entering into agreement to acquire share, voting rights or control over the Target Company.
13(2)(a)	Market Purchase of shares	Prior to the placement of purchase order with the stock broker.
13(2)(b)	Acquisition pursuant to conversion of Convertible Securities without a fixed date of conversion or upon conversion of depository receipts for the underlying shares	On the same day when the option to convert such securities into shares is exercised.
13(2)(c)	Acquiring shares or voting rights or control pursuant to conversion of Convertible Securities with a fixed date of conversion	On the second working day preceding the scheduled date of conversion of such securities into shares.
13(2)(d)	In case of disinvestment	On the date of execution of agreement for acquisition of shares or voting rights or control over the Target Company.
13(2)(e)	In case of Indirect Acquisition where the parameters mentioned in Regulation 5(2) are not met	Within four working days of the following dates, whichever is earlier: a. When the primary acquisition is contracted; and b. Date on which the intention or decision to make the primary acquisition is announced in the public domain.

13(2)(f)	In case of Indirect Acquisition where the parameters mentioned in Regulation 5(2) are met	On the same day of the following dates, whichever is earlier: a. When the primary acquisition is contracted; and b. Date on which the intention or decision to make the primary acquisition is announced in the public domain.
13(2)(g)	Acquisition of shares, voting rights or control over the Target Company pursuant to Preferential Issue	On the date when the board of directors of the target company authorizes such preferential issue
13(2)(h)	Increase in voting rights pursuant to a buy-back not qualifying for exemption under Regulation 10	Not later than 90 th day from the date of closure of the buy-back offer by the target company.
13(2)(i)	Acquisition of shares, voting rights or control over the Target Company where the such acquisition is beyond the control of acquirer	Not later than two working days from the date of receipt of such intimation.
13(3)	Voluntary Offer	On the same day when the Acquirer decides to make Voluntary Offer
14(1)	Public Announcement shall be sent to all the stock exchanges and same information disseminate to public	On the same day
14(2)	Public Announcement shall also sent to Board of Directors and Target Company at its Registered Office	One working day of the date of the public announcement
14(3)	Detailed Public Statement pursuant to the public announcement shall be published in all Editions of any one of English Newspaper, any one Hindi Newspaper and any one Regional Language newspaper. Where registered office of company and any one Regional Language Newspaper at place of stock exchange where highest volume traded in preceding 60 days.	Within 5 working days from the date of Public Announcement
14(4)	Such detailed public statement in the newspapers, a copy of the same shall be sent a) SEBI; b) All the stock exchanges on which the shares of the target company are listed	Immediately

	c) the target company at its registered office	
16	Submission of Letter of Offer to SEBI with non-refundable fees	within 5 working days from the date of detailed public announcement
17	Opening of Escrow Account	Not later than two working days prior to the date of the detailed public statement of the open offer for acquiring shares
18(1)	The acquirer shall send a copy of the draft letter of offer to the target company at its registered office address and to all stock exchanges where the shares of the target company are listed.	Immediately
18(2)	The letter of offer shall be dispatched to the shareholders whose names appear on the register of members of the target company as of the identified date	not later than seven working days from the receipt of comments from SEBI or where no comments are offered by SEBI, within seven working days from the expiry of the period stipulated in regulation 16(4)
18(3)	The acquirer shall send the letter of offer to the custodian of shares underlying depository receipts, if any, of the target company.	Immediately
18(8)	Opening of the offer	not later than 12 working days from date of receipt of comments from SEBI and shall remain open for 10 working days
18(10)	Completion of requirements relating to the Open Offer tendering period	Within 10 working days from the last date of the tendering period
	EVENT BASED DISCLOSURES	
	Disclosure of Acquisition and Disposal	
29(1)	When an Acquirer together with PAC acquires 5% or more in aggregate of the shares or voting rights of the target company (together with the existing shares or voting rights held by them) shall disclose to Stock Exchange & Target Company	Within 2 working days of the receipt of intimation of allotment of shares or acquisition of shares or voting rights
29(2)	When an Acquirer together with PAC holding 5% or more in a target company shall disclose every acquisition or disposal of shares representing 2% or more of the shares or voting rights.	Within 2 working days of the receipt of intimation of allotment of shares or disposal or acquisition of shares or voting rights

	ANNUAL DISCLOSURES	
	Continual disclosures	
30(1)	Acquirer with PAC holding 25% or more shares or voting rights to Stock Exchange and Target Company	Within seven working days from the end of each financial year i.e., 31 March
30(2)	Promoter with PAC shall disclose their aggregate shareholding to the stock Exchange and Target	Within seven working days from the end of each financial year i.e., 31 March
	DISCLOSURE OF ENCUMBERED SHARES	
31(1)	A Promoter shall disclose details of shares in such target company encumbered by him or by PAC's with him	Within 7 working days from the creation or invocation or release of encumbrance as the case may be
31(2)	A Promoter shall disclose details of invocation of such encumbrance or release of such encumbrance of shares	Within 7 working days from the creation or invocation or release of encumbrance as the case may be

LESSON ROUND UP

- SAST aims at protecting interest of the investors in securities of a listed company providing amongst others, an opportunity for the public shareholders to exit where there is a substantial acquisition of shares or voting rights or control over a listed company, consolidation of holdings by existing shareholders and related disclosures and penalties for non- compliance etc.
- The Takeover Regulations, 1997 stand repealed from October 22, 2011, i.e. the date on which SAST Regulations, 2011 come into force.
- SEBI Takeover Regulations, 2011 provides certain trigger events wherein the Acquirer is required to give Open Offer to the shareholders of the Target Company to provide them exit opportunity.
- Regulation 6 of the Takeover Regulations provides the threshold and conditions for making the Voluntary Open Offer.
- An offer in which the acquirer has stipulated a minimum level of acceptance is known as a conditional offer.
- Regulation 10 & 11 provides for automatic exemptions and exemptions by SEBI.
- The public announcement shall be sent to all the stock exchanges on which the shares of the target company are listed, and the stock exchanges shall forthwith disseminate such information to the public.
- In SEBI Takeover Regulations, 2011, the obligation to give the disclosures on the acquisition of certain limits is only on the acquirer and not on the Target Company.

GLOSSARY

Competitive Bid	An offer made by a person other than the acquirer who has made the first public announcement.
Control of management	The right to appoint directly or indirectly or by virtue of agreements or in any other manner majority of directors on the Board of the target company or to control management or policy decisions affecting the target company.
Corporate restructuring	Involves making radical changes in the composition of the businesses in the company's portfolio.
Disinvestment	Disinvestment means the direct or indirect sale by the Central Government or any State Government or by a government company, as the case may be, of shares or voting rights in, or control over, a target company, which is a public sector undertaking;
Encumbrance	It shall include a pledge, lien or any such transaction, by whatever name called.
Public Announcement	A public announcement is an announcement made in the newspapers by the acquirer primarily disclosing his intention to acquire shares of the target company from existing shareholders by means of an open offer.
Takeover	Takeover is a corporate device whereby one company acquires control over another company, usually by purchasing all or majority of its shares.
Weighted average number of total shares	Weighted average number of total shares means the number of shares at the beginning of a period, adjusted for shares cancelled, bought back or issued during the aforesaid period, multiplied by a time-weighting factor;

SELF TEST QUESTIONS

(These are meant for re-capitulation only. Answers to these questions are not to be submitted for evaluation.)

1. What is the meaning of Person acting in concert under SEBI (SAST) 2011 Regulations?
2. What are the conditions for making Voluntary open offer?
3. What are the provisions relating to Public announcement under the Takeover regulations?
4. Discuss about the continuous Disclosure required to be made under these regulations.
5. Briefly explain the conditions on which SEBI can grant exemption to an acquirer.
6. What do you mean by creeping acquisition
7. Briefly explain the provisions relating to Escrow Account.

Lesson 24

Investor Protection

LESSON OUTLINE

- Introduction
- Legal Framework for Investor Protection in India
- Investor Education and Protection Fund
- SEBI (Investor Protection and Education Fund) Regulation, 2009
- Financial Education
- Investors' rights and responsibilities
- Types of Grievances and Dealing Authorities
- Initiatives taken so far on Financial Literacy in India
- Investor Grievance Redressal Mechanism at SEBI
- SCORES (SEBI Complaints Redress System)
- SEBI (Informal Guidance)Scheme, 2003
- LESSON ROUND UP
- GLOSSARY
- SELF-TEST QUESTIONS

LEARNING OBJECTIVES

Investor protection is one of the most important elements of a thriving securities market or other financial investment institution. Investor protection focuses on making sure that investors are fully informed about their purchases, transactions and the affairs of the company that they have invested in.

Investors protection is a very popular phrase with all these concerned with regulation of the capital market, stock exchanges, SEBI, MCA, RBI, Investors Association, or matter of fact the companies themselves – Various Procedures, Guidelines, Rules and Regulations have been issued in the Legislations to protect the Investor's right and repose the confidence.

Keeping the above in view, this lesson will enable the students to understand the concept and need for Investor Protection and Education, Rights and responsibilities of investors, legal framework for investor protection in India, measures and initiative, taken for financial literacy in India and SEBI SCORES system.

INTRODUCTION

The securities market operations promote the economic growth of the country. More efficient is the securities market, the greater is the promotion effect on economic growth. It is, therefore, necessary to ensure that securities market operations are more efficient, transparent and safe. In this context, the investors need protection from the various malpractices and unfair practices made by the corporate and intermediaries. As the individual investors' community and the investment avenues are on the rise, it is interesting to know how the investors shall be protected through various legislations. Securities market in general are to be regulated to improve the market operations in fair dealings and easy to access the market by corporate and investors. The present positive attitude of investors is heartening though investor sentiments have been shaken by the various scandals. Even though, there are various opportunities available for investment, investors are scared of investing. In this situation, the individual investors' protection becomes necessary to sustain the economic development of the country.

The desired level of economic growth of a country is dependent upon availability of protection to its investors'. Globally, there is increased evidence to suggest that investor protection has assumed an important role in the economic development of a country. Integrity of the financial markets and economic well being of the country depend on corporate accountability and investors confidence. The global concern to make capital markets safer and transparent can be achieved by strengthening financial system and managing the crisis efficiently. The revival of investors' protection in the corporate securities market is necessary to make market more efficient by means of converting savings to investment. If the investors are not protected properly by way of providing fair rate of return and safeguarding their capital, the corporate will not be able to mobilize funds from the market at reasonable rate in times to come. In view of the foregoing with a view to gain the confidence of investors in the securities market it is necessary to provide adequate rate of return on investors' capital by corporates through their operational efficiency. This will enable us to lure back investors to the capital market. This can be done by a series of systematic measures which would build their confidence in the systems and processes and protect the interest of investors.

INVESTORS' RIGHTS AND RESPONSIBILITIES

Equity shareholders are the real owner of the company and with the growth of the company equity shareholders also get capital appreciation, vice versa is also true. Investment in equity shares cannot be guaranteed with any income and/or growth. Following are the rights and responsibilities of a shareholder of a company :

The Rights of Investor as a shareholder

- To receive the share certificates, on allotment or transfer (if opted for transaction in physical mode) as the case may be, in due time. Now in case of Public Issue investors will be allotted shares in dematerialized mode only and subsequently they can rematerialized the allotted shares.
- To receive copies of the Annual Report containing the Balance Sheet, the Profit & Loss account and the Auditor's Report.
- To participate and vote in general meetings either personally or through proxy.
- To receive dividends in due time once approved in general meetings.
- To receive corporate benefits like rights, bonus, etc. once approved.
- To apply to National Company Law Tribunal (NCLT) to call or direct the calling of an Annual General Meeting.
- To inspect the minute books of the general meetings and to receive copies thereof.
- To proceed against the company by way of civil or criminal proceedings.
- To apply for the winding up of the company.

- To receive the residual proceeds in case of winding up.
- To receive offer to subscribe to right share in case of further issue of shares.
- To receive offer in case of Takeover or Buy-back under SEBI Regulations.
- Besides the above rights, which investors enjoy as an individual shareholder, investors also enjoy the following rights as a group:
 - (a) To give requisition for an Extra-ordinary General meeting.
 - (b) To demand a poll on any resolution.
 - (c) To apply to NCLT to investigate into the affairs of the company.
 - (d) To apply to NCLT for relief in cases of oppression and/or mismanagement.

Rights of Investors as a debenture holder

- To receive interest on redemption of debentures in due time.
- To receive a copy of the trust deed on request.
- To apply for winding up of the company if the company fails to pay its debt.
- To approach the Debenture Trustee with your grievance.
- You may note that the above mentioned rights may not necessarily be absolute. For example, the right to transfer securities (in physical mode) is subject to the company's right to refuse transfer as per statutory provisions.

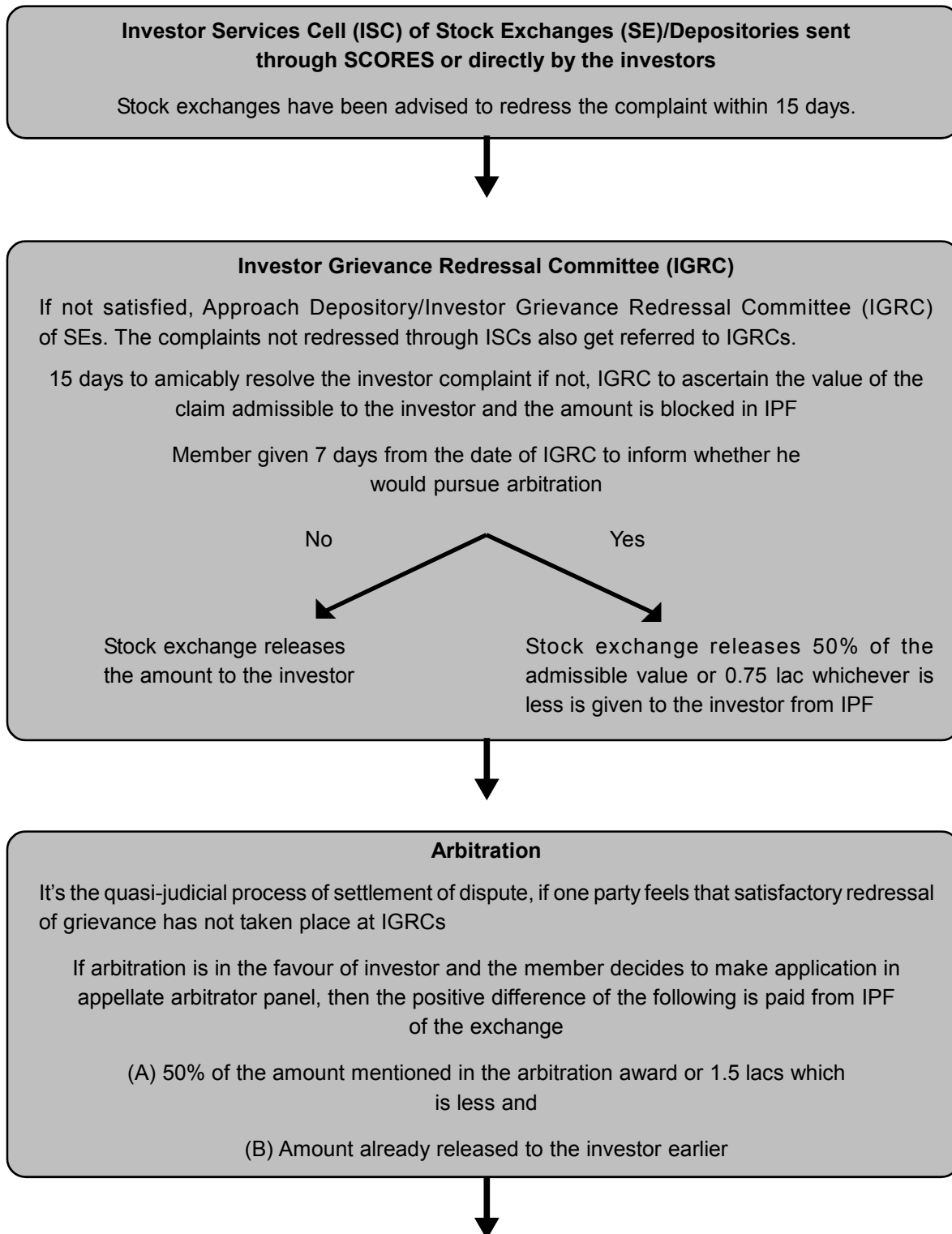
Responsibilities of an Investor as a security holder

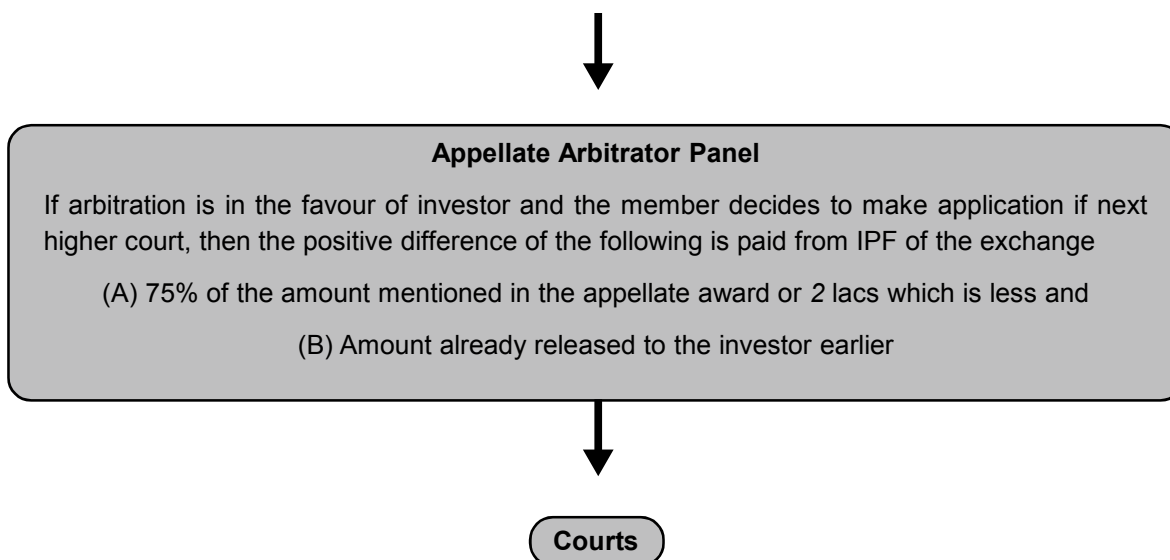
- To be specific
- To remain informed
- To be vigilant
- To participate and vote in general meetings
- To exercise your rights on your own or as a group.

WHOM TO APPROACH FOR COMPLAINT AGAINST STOCK BROKERS/DEPOSITORY PARTICIPANTS

Investors who are not satisfied with the response to their grievances received from the brokers/Depository Participants/listed companies, can lodge their grievances with the Stock Exchanges or Depositories. The grievance can be lodged at any of the offices of the BSE/NSE located at Chennai, Mumbai, Kolkata and New Delhi. In case of unsatisfactory redressal, BSE/NSE has designated Investor Grievance Redressal Committees (IGRCs), or Regional Investor Complaints Resolution Committees (RICRC), this forum acts as a mediator to resolve the claims, disputes and differences between entities and complainants. Stock Exchanges provide a standard format to the complainant for referring the matter to IGRC/RICRC. The committee calls for the parties and acts as a nodal point to resolve the grievances. For any detailed information, please visit the website of the respective stock exchange. If the grievance is still not resolved, an investor can file arbitration under the rules, bye laws and regulations of the respective Stock Exchange/Depository.

Grievance redressal mechanism at stock exchange





- Undertaking given by the investor to stock exchange to return the amount released to him, in case the proceedings are decided against the investor or he decides not to pursue further.
- Total amount released to the investor through monetary relief shall not exceed Rs.5 lac in one financial year
- In case of non-payment of the amount by the investor, trading not allowed on any stock exchange and demat account shall be frozen.

What is Arbitration

- Arbitration is a quasi judicial process of settlement of disputes between investors and trading members (brokers)/sub-brokers or within brokers themselves. It aims at quicker legal resolution of disputes for all the transactions done on the exchange. The arbitration framework is governed by rules byelaws, circulars and regulations issued by the exchange(s) and SEBI from time to time.

Important points to remember in arbitration

- The complaint in the other systems shall be treated as closed, once arbitration proceeding are initiated since it is quasi judicial process.
- Arbitrator application to be filed within three years from incidence. (Law of limitation)
- Choice of selecting arbitrator(s) from the common pool of arbitrators of all the exchanges together; or else system generated.
- A panel of three arbitrators, if the value of claim is > 25 lakh; and sole arbitrator if < 25 lakhs.
- No deposit fees for claims upto to 10 lakhs for the investor
- Appeal within 30 days to the Appellate Arbitrators panel
- Filing of petition in the competent court nearest to the investor's residence.
- The fees for appeal shall not exceed Rs. 10,000/-, in addition to statutory charges if the claim/counter claim is upto 10 lakh.

For more details, visit 'investor' section of exchange/depositories websites.

TYPES OF GRIEVANCES AND DEALING AUTHORITY

Grievances pertaining to	Regulator
Banks deposits and banking Fixed Deposits with Non Banking Financial Companies (NBFCs) and other matters pertaining to NBFCs Primary Dealers	Reserve Bank of India (RBI) http://www.rbi.org.in/
Fixed Deposits with manufacturing companies Unlisted companies Mismanagement of companies, financial performance of the company, Annual General Meeting, Annual Report, minority shareholders interest, non-receipt of preferential allotment shares, etc. and corporate actions as per the court order such as mergers, amalgamation, reduction of share capital/par value, etc. Nidhi Companies	Ministry of Corporate Affairs (MCA) http://www.mca.gov.in/
Insurance Companies/Brokers /Agents/products and Service	Insurance Regulatory and Development Authority India (IRDA) http://www.irdai.gov.in/
Commodities	Forward Markets Commission (FMC) http://www.fmc.gov.in/
Pension fund	Pension Fund Regulatory and Development Authority (PFRDA) http://www.pfrda.org.in/
Monopoly and anti competitive practices	Competition Commission of India (CCI) http://www.cci.gov.in/
Chit Funds	Registrars of Chit Funds of the concerned State.
Housing Finance Companies	National Housing Bank (NHB) www.nhb.org.in

LEGAL FRAMEWORK FOR INVESTOR PROTECTION IN INDIA

In order to afford adequate protection to the investors, provisions have been incorporated in different legislations such as the Companies Act, Securities Contracts (Regulation) Act, Consumer Protection Act, Depositories Act, and Listing Agreement of the Stock Exchanges supplemented by many guidelines, circulars and press notes issued by the Ministry of Finance, Ministry of Corporate Affairs and SEBI from time to time. The legislations as well as the rules and regulations notified thereunder specify disclosure requirements to be complied with by the companies and also punishments and remedies for failure of compliance.

1. COMPANIES ACT, 2013**Acceptance of Deposits**

Section 73(1) - This section provides that no Company shall accept or review deposit under this Act from the

public except in a manner provided under Chapter V (Acceptance of Deposits by Companies) of Companies Act, 2013 and Companies (Acceptance of Deposits) Rules, 2014 made thereunder.

In terms of sub section 4, where a Company fails to repay the deposit or part thereof, or any interest thereon the deposit for concerned may apply to the Tribunal for an order directing the company to pay the sum due or for any loss or damage incurred by him as a result of such non-payment and for such other orders as the Tribunal may deem fit.

Sub-section 3 of section 74 lays down that if a company fails to repay the deposit or part thereof or any interest thereon within the time specified under section 74 or such further times as may be allowed by the Tribunal, the company shall, in addition to the payment of the amount of deposit or part thereof and the interest due, be punishable with fine which shall not be less than one crore rupees and which may extend to ten crore rupees and every officer of the company who is in default shall be punishable with imprisonment which may extend to seven years or with fine which shall not be less than twenty five lakh rupees and which may extend to two crore rupees, or with both.

Rule 21 of Companies (Acceptance of Deposits) Rules, 2014 stipulates that if any company referred to in sub-section (2) of section 73 or any eligible company inviting deposits or any other person contravenes any provisions of these rules for which no punishment is provided in the act, the company and every officer of the company who is in default shall be punishable with fine which may extend to five thousand rupees and where the contravention is a continuing one, with a further fine which may extend to five thousand rupees for every day after the first day during which the contraventions continue.

Mis-statements in Prospectus

Section 34 deals with criminal liability for mis-statement in prospectus issued by a company.

Section 34: Where a prospectus, issued, circulated or distributed, includes any statement which is untrue or misleading in form or context in which it is included or where any inclusion or omission of any matter is likely to be mislead, every person who authorises the issue of such prospectus shall be liable for action under section 447.

Section 447: Any person who is found to be guilty of fraud, shall be punishable with imprisonment for a term which shall not be less than six months but which may extend to ten years and shall also be liable to fine which shall not be less than the amount involved in the fraud, but which may extend to three times the amount involved in the fraud. However, where the fraud in question involves public interest the terms of the imprisonment shall not be less than three years.

Fraudulently inducing persons to invest money

Section 36: Any person who, either knowingly or recklessly makes any statement, promise or forecast which is false, deceptive or misleading, or deliberately conceals any material facts, to induce another person to enter into, or to offer to enter into-

- (a) any agreement for, or with a view to, acquiring, disposing of, subscribing for or underwriting, securities; or
- (b) any agreement the purpose or the pretended purpose of which is to secure a profit or any of the parties from the yield of securities or by reference to fluctuations in the value of securities; or
- (c) any agreement, for, or with a view to, obtaining credit facilities from any bank or financial institution,

shall be liable for action under section 447.

Punishment for Personation for acquisitions, etc., of securities

Section 38: Any person who –

- (a) makes or abets making an application in a fictitious name to a company for acquiring, or subscribing for, its securities; or
- (b) makes or abets making of multiple applications to the company in different names or in different combinations of his name or surname for acquiring or subscribing for its securities; or
- (c) otherwise induces directly or indirectly a company to allot, or register any transfer thereof, securities to him, or to any other person in a fictitious name,

shall be liable for action under section 447.

Non-payment of Dividend

Section 123: This section, inter alia, requires a company who has declared a dividend for any financial year to deposit the amount of such dividend (including interim dividend) in a scheduled bank in a separate account within 5 days from the date of declaration of such dividend.

Section 124: This section provides that where a dividend has been declared by a company which has not been paid or claimed within 30 days from the date of such declaration, the company shall within 7 days of expiry of the said period of 30 days transfer the total amount of dividend which remains unpaid or unclaimed to a special account to be opened by a company in this behalf in any scheduled bank to be called the unpaid dividend account.

This section also provide for penalty for non complying with the above requirement and the same by way of interest @ 12% per annum and the interest accruing on the amount of unpaid/unclaimed dividend not transferred to the unpaid dividend account.

Section 125: This section provides for establishment of Investors' Education and Protection Fund by the Central Government. Various types of unpaid/unclaimed amounts of application money/matured deposits/matured debenture etc., are to be credited to the said fund. The said accumulation in this fund are to be utilized for promotion of investors' awareness and protection of investors' interests.

Further, if a company fails to comply with any of the requirements of Section 124, the company shall be punishable with fine which shall not be less than five lakh rupees but which may extend to twenty five lakh rupees and every officer of the company who is in default shall be punishable with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees.

Transfers and Transmission of Securities

Regarding transfers and transmissions of securities necessary provisions are available in Section 56, 58, 59 of the Companies Act, 2013. As regards listed companies, the clauses in the listing agreement contain provisions for prompt issue of certificates after effecting transfers.

Failure to comply with the provisions of Companies Act, 2013 can be brought before the Tribunal through an appeal under Section 58 and 59. After hearing the parties the Tribunal may by order direct the company to register the transfer.

Failure to Send Financial Statements

Section 136: This section provides for the right of a member to obtain copies of balance sheet and auditors report.

Sub-section 3 provides that in case of default complying with this requirement, the company shall be liable for a penalty of twenty five thousand rupees and every officer who is in default shall be liable to a penalty of five thousand rupees.

Besides, Section 436 permits the shareholder to proceed against the company and its officers in a court of law generally for offences committed under the Companies Act including prospectus, abridged prospectus, allotment, listing, transfer of shares, dividend payment etc. committed by the company as well as its officers under various provisions in the Act.

Protection to Debenture-holders

Section 71 of the Companies Act, 2013 protects the debenture holders and contains stringent penalties for default and also empowers the debenture trustee to make an appeal to the Tribunal.

2. SEBI ACT, 1992

The securities market enable capital formation in the economy and enhances wealth of investors who make the right choices. The investor confidence is the key prerequisite for the emergence of a vibrant and deep capital market. The role of regulator in creating and enhancing investors confidence is therefore paramount. Accordingly SEBI was set up by an Act on Parliament in April 1992 with a mandate to:

- Protect the interest of investors
- Promote the development of and
- To regulate the securities market.

Section 11 in Chapter IV of the SEBI Act lists out the functions of the SEBI. Section 11(2)(e) stipulates prohibition of fraudulent and unfair practices relating to securities markets as one of these functions and Section 11(2)(g) provides for prohibition of insider trading in securities. In pursuance of this provision SEBI had notified the SEBI (Prohibition of fraudulent and unfair practices relating to securities markets) Regulations, 1995 on 25th October, 1995 which have now been replaced with SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 2003 w.e.f. 17.7.2003.

Section 15A to Section 15HA provide for penalty in respect of failure to furnish information, return, etc., failure by any person to enter into agreement with clients, failure to redress investors' grievances, certain defaults in case of mutual funds, failure to observe rules and regulations by an asset management company, default in case of stock brokers, insider trading, non-disclosure of acquisition of shares and takeovers, fraudulent and unfair trade practices.

Section 24 provides for punishment with imprisonment upto 10 years or with fine which may extend to ₹ 25 crores or with both. If any person contravenes or attempts to contravene or abets the contravention of the provision of SEBI Act or any rules or regulation.

As regards violation of provisions in the listing agreement, investors can forward their complaints to the stock exchanges with whom the company is listed to initiate action. The Investors are also at liberty to file complaints before the District Forum, State Commission or National Commission established under Section 9 of the Consumer Protection Act.

In the case of listed companies, investors are entitled to forward their complaints to the company and SEBI and the latter takes up the matter with the companies. SEBI has the power to take action including criminal proceeding where necessary against persons responsible for delay.

3. SECURITIES CONTRACTS (REGULATION) ACT, 1956

Section 23 provides for penalties which may extend to 10 years or with fine which may extend to ₹ 25 crores or with both for contravention of the provisions of the Act.

Section 23A to Section 23H provide for penalty in respect of failure to furnish information, return etc., failure by any person to enter into an agreement with clients, failure to redress investor grievances, failure to segregate securities or moneys of client or clients, failure to comply with provisions of listing conditions or delisting conditions or grounds, excess dematerialization or delivery of unlisted securities, failure to furnish periodical returns, contravention with any provision of the act where no separate penalty is provided.

Section 23M provides for penalty for imprisonment for a term which may extend to 10 years or with fine which may extend to ₹ 25 crore or both for contravention or attempts to contravene or abates the contravention of the provisions of the Act or any rules or regulations or bylaws.

4. RESERVE BANK OF INDIA ACT, 1938

Section 45 QA of the Reserve Bank of India Act gives a depositor similar rights as are provided under Companies Act to approach Tribunal for payment of matured deposits in the case of NBFCs.

5. INDIAN PENAL CODE

Economic Offence Wings of the Police Departments have powers under IPC to take up the cases of cheating, forgery and misappropriation etc., relating to investments.

Stock exchanges can also take up the issues pertaining to securities in terms of the conditions of listing agreement, rules and regulations.

INVESTOR EDUCATION AND PROTECTION FUND

Investor Education and Protection Fund (IEPF) has been established under Section 125 of the Companies Act, 2013, for promotion of investors' awareness and protection of the interests of investors. The Ministry of Corporate Affairs (MCA) vide its notification dated 13th January, 2016 notified the provisions of section 125 of the Companies Act, 2013. The Ministry of Corporate Affairs (MCA) vide Notification dated 5 September, 2016 has also notified the Investor Education and Protection Fund Authority (Accounting, Audit, Transfer & Refund) Rules 2016, which are effective from 7 September, 2016.

SECTION 125 OF THE COMPANIES ACT, 2013

Section 125 of the Companies Act, 2013 read with Investor Education and Protection Fund Authority (Accounting, Audit, Transfer and Refund) Rules, 2016 provides the provisions for establishment of a Fund which is called the Investor Education and Protection Fund.

Amount to be credited

As per section 125(2) of the Act, the following amount is required to be credited to the Fund (IEPF):-

- a) the amount given by the Central Government by way of grants after due appropriation made by Parliament by law in this behalf for being utilised for the purposes of the Fund;
- b) donations given to the Fund by the Central Government, State Governments, companies or any other institution for the purposes of the Fund;
- c) the amount in the Unpaid Dividend Account of companies transferred to the Fund under sub-section (5) of section 124;
- d) the amount in the general revenue account of the Central Government which had been transferred to that account under sub-section (5) of section 205A of the Companies Act, 1956 (1 of 1956), as it stood immediately before the commencement of the Companies (Amendment) Act, 1999 (21 of 1999), and remaining unpaid or unclaimed on the commencement of this Act;
- e) the amount lying in the Investor Education and Protection Fund under section 205C of the Companies Act, 1956;
- f) the interest or other income received out of investments made from the Fund;
- g) the amount received under sub-section (4) of section 38;
- h) the application money received by companies for allotment of any securities and due for refund;
- i) matured deposits with companies other than banking companies;
- j) matured debentures with companies;

- k) interest accrued on the amounts referred to in clauses (h) to (j);
- l) sale proceeds of fractional shares arising out of issuance of bonus shares, merger and amalgamation for seven or more years;
- m) redemption amount of preference shares remaining unpaid or unclaimed for seven or more years; and
- n) such other amount as may be prescribed.

As per Rule 3(2) of IEPF Authority (Accounting, Audit, Transfer and Refund) Rules, 2016 provides the following additional amounts to be credited in the Fund:-

- a) all amounts payable as mentioned in clause (a) to (n) of sub-section (2) of section 125 of the Act;
- b) all shares in accordance with sub-section (6) of section 124 of the Act;
- c) all the resultant benefits arising out of shares held by the Authority under clause (b);
- d) all grants, fees and charges received by the Authority under these rules;
- e) all sums received by the Authority from such other sources as may be decided upon by the Central Government;
- f) all income earned by the Authority in any year;
- g) all amounts payable as mentioned in sub-section (3) of section 10B of the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970 and section 10B of Banking Companies (Acquisition and Transfer of Undertakings) Act, 1980; and
- h) all other sums of money collected by the Authority as envisaged in the Act.

Utilisation of Fund

As per section 125(3) of the Act, the following amount shall be utilised for –

- a) the refund in respect of unclaimed dividends, matured deposits, matured debentures, the application money due for refund and interest thereon;
- b) promotion of investors' education, awareness and protection;
- c) distribution of any disgorged amount among eligible and identifiable applicants for shares or debentures, shareholders, debenture-holders or depositors who have suffered losses due to wrong actions by any person, in accordance with the orders made by the Court which had ordered disgorgement;
- d) reimbursement of legal expenses incurred in pursuing class action suits under sections 37 and 245 by members, debenture-holders or depositors as may be sanctioned by the Tribunal; and
- e) any other purpose incidental thereto,

in accordance with such rules as may be prescribed:

However, the person whose amounts referred to in clauses (a) to (d) of sub-section (2) of section 205C transferred to IEPF, after the expiry of the period of seven years as per provisions of the Companies Act, 1956, shall be entitled to get refund out of the fund in respect of such claims in accordance with rules made under this section.

Explanation – The disgorged amount refers to the amount received through disgorgement or disposal of securities.

Any person can claim the amount specified in section 125(2), he shall apply to the authority constituted by Central Government by making an application in Form IEPF 5 online available on website www.iepf.gov.in along with fee, as decided by the Authority from time to time in consultation with the Central Government, under his own signature.

The Central Government by notification, shall constitute an authority for administration of the Fund consisting of a chairperson and such other members, not exceeding seven and a chief executive officer, as the Central Government may appoint. The manner of administration of the Fund, appointment of chairperson, members and chief executive officer, holding of meetings of the authority shall be in accordance with IEPF Authority (Appointment of Chairperson and Members, holding of meetings and provision for offices and officers) Rules, 2016.

The accounts of the Fund shall be audited by the Comptroller and Auditor- General of India at such intervals as may be specified by him and such audited accounts together with the audit report thereon shall be forwarded annually by the authority to the Central Government.

SEBI (INVESTOR PROTECTION AND EDUCATION FUND) REGULATIONS, 2009

SEBI in exercise of the powers conferred by section 30 of SEBI Act, 1992, SEBI made the SEBI (Investor Protection and Education Fund) Regulations, 2009.

Regulation 3 of the Act lays down the establishment of the fund which shall be called the Investor Protection and Education Fund.

Regulation 4 provides for the amounts to be credited to the Fund. The following amounts shall be credited to the Fund:

- (a) contribution as may be made by SEBI to the Fund;
- (b) grants and donations given to the Fund by the Central Government, State Government or any other entity approved by SEBI for this purpose;
- (c) proceeds in accordance with the sub-clause (ii) of clause(e) of sub-regulation (10) of regulation 17 and the sub- regulation (3) of regulation 21 of SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011;
- (d) security deposits, if any, held by stock exchanges in respect of public issues and rights issues, in the event of de-recognition of such stock exchanges;
- (e) amounts in the Investor Protection Fund and Investor Services Fund of a stock exchange, in the event of de-recognition of such stock exchange;
- (f) amounts forfeited for non-fulfilment of obligations specified in regulation 15B of the SEBI (Buy-back of Securities) Regulations, 1998;
- (g) monies transferred in accordance with sub-regulation (9) of regulation 45 of the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009;
- (h) amounts disgorged under section 11B of the Act or section 12A of the Securities Contracts (Regulation) Act, 1956 or section 19 of the Depositories Act, 1996
- (i) interest or other income received out of any investments made from the Fund;
- (j) such other amount as SEBI may specify in the interest of investors.

Explanation to Regulation 4(g) of SEBI (Investor Protection and Education Fund) Regulations, 2009, any proceeds due to:

(a) Disinvestment:

In case a custodian is unable to deliver the securities or ascertain the claimant for the securities that are received subsequent to write off due to any unforeseen circumstances viz. deemed Foreign Portfolio Investor/Foreign Portfolio Investor no longer existing/operating or expiry of SEBI registration/FEMA approval, etc., the sale of these securities through stock exchange and proceeds thereof net of expenses shall be credited to the Investors Protection and Education Fund of SEBI not later than 7 days from the date of receipt thereof.

(b) Corporate benefits:

In case of receipt of corporate benefits in the form of securities arising out of shares written off, the same shall be reported to SEBI in the normal manner. Similarly, corporate benefits received in the form of cash viz. dividend shall be credited to the Investors Protection and Education Fund of SEBI not later than 7 days from the date of receipt of the same.

Above mentioned amount shall be credit to the Fund through NEFT/RTGS/IMPS or any other mode allowed by RBI or by way of a demand draft in favour of the SEBI payable in Mumbai.

Utilisation of Fund

The fund shall be utilised for the purpose of protection of investors and promotion of investor education and awareness in accordance with these regulations. The fund may be used for the following purposes, namely:-

- (a) Educational activities including seminars, training, research and publications, aimed at investors;
- (b) Awareness programmes including through media - print, electronic, aimed at investors;
- (c) Funding investor education and awareness activities of Investors' Associations recognized by SEBI
- (d) Aiding investors' associations recognized by SEBI to undertake legal proceedings in the interest of investors in securities that are listed or proposed to be listed;
- (e) Refund of the security deposits which are held by stock exchanges and transferred to the Fund consequent on de-recognition of the stock exchange, in case the concerned companies apply to SEBI and fulfill the conditions for release of the deposit;
- (f) Expenses on travel of members of the Committee, who are not officials of the Board, and special invitees to the meetings of the Committee, in connection with the work of the Committee;
- (g) Salary, allowances and other expenses of office of Ombudsman; and
- (h) Such other purposes as may be specified by SEBI.

The amount disgorged and credited to the fund in accordance with clause (h) of regulation 4 and the interest accrued thereon shall, in cases when SEBI deems fit to make restitution to eligible and identifiable investors who have suffered losses resulting from violation of securities Law, be utilised for the purposes of such restitution. However, the money left in the fund after earmarking the amount for the process of restitution to eligible and identifiable investors may be utilised for the purposes of the fund specified in the regulation. Further, no claim for restitution from the disgorged amounts in specified case shall be adjustable after a period of seven years from the date of invitation of claim for disgorgement in the said case by SEBI.

Conditions for Aid

The aid shall be given by SEBI to investors' associations, in accordance with the guidelines made by it and subject to the following conditions:

- (a) that the aid shall not exceed seventy five per cent of the total expenditure on legal proceedings;
- (b) such aid shall not be considered for more than one legal proceeding in a particular matter;
- (c) if more than one investors' association applies for seeking legal aid, the investors' association whose application is received first, shall be considered for such aid.

Constitution of The Committee

SEBI shall constitute an advisory committee for recommending investor education and protection activities that may be undertaken directly by SEBI or through any other agency, for utilisation of the Fund for the purposes referred in these regulations. The Committee shall consist of the following members, namely:-

- (a) The Executive Director of SEBI in charge of Office of Investor Assistance and Education who shall be the convener of the Committee;
- (b) Two other officials of SEBI;
- (c) Five other members who have expertise about the securities market and experience in matters of investor grievance redressal or investor education.

The term of office of members shall be two years, which may be extended for a further period of two years. Any vacancy arising out of resignation, retirement or death of a member or for any other reason shall be filled by SEBI for the remaining period of the term of such member. SEBI may dissolve and reconstitute the Committee if, at any time, SEBI is of the opinion that the Committee is unable to discharge the functions and duties imposed on it by or under these regulations.

FINANCIAL EDUCATION

An increased need for financial education is felt in both developed and developing countries. In developed countries, the increasing number of financial products, its complexity, importance of retirement savings, increased growth of secondary market has made the imparting of financial education imperative for all age groups, including students so that individuals are educated about financial matters as early as possible in their lives. In the developing countries, the growing number of investors, technically advanced financial markets, liberalised economy etc., necessitates imparting of financial education for better operation of markets and economy and in the interest of investor. Further imparting of financial education is international concern due to growth of international transactions, international financial instruments like ADR, GDR, IDR etc., mobility of individuals from one country to another etc.

INITIATIVES TAKEN SO FAR ON FINANCIAL LITERACY IN INDIA

RBI's initiatives

Reserve Bank of India has undertaken a project titled "Project Financial Literacy". The objective of this project is to disseminate information regarding the central bank and general banking concepts to various target groups, including school and college students, women, rural and urban poor, defense personnel and senior citizens. The project envisages a multi pronged approach. The project has been designed to be implemented in two modules, one module focusing on the economy, RBI and its activities, and the other module on general banking. The material is created in English and other vernacular languages. It is disseminated to the target audience with the help of banks, local government machinery, schools and colleges through presentations, pamphlets, brochures, films and also through RBI's website.

SEBI Initiatives

Securities and Exchange Board of India has embarked financial education on a nationwide campaign. To undertake financial education to various target segments viz. school students, college students, working executives, middle income group, home makers, retired personnel, self help groups etc., SEBI has empanelled Resource Persons throughout India. The Resource Persons are given training on various aspects of finance and equipped with the knowledge about the financial markets. These SEBI Certified Resource Persons organise workshops to these target segments on various aspects viz. savings, investment, financial planning, banking, insurance, retirement planning etc.

Investor education programs are conducted by SEBI through investor associations all over the country. Regional seminars are conducted by SEBI through various stakeholders viz. Stock Exchanges, Depositories, Mutual Funds Association, Association of Merchant Bankers etc. SEBI has a dedicated website for investor education wherein study materials are available for dissemination. SEBI also publishes study materials in English and vernacular languages. Under "Visit SEBI" programme, School and college students are encouraged to visit

SEBI and understand its functioning. SEBI has recently set up SEBI Helpline in 14 languages wherein through a toll free number, investors across the country can access and seek information for redressal of their grievances and guidance on various issues.

Ministry of Corporate Affairs (MCA) Initiatives

Financial literacy allows to fully appreciate opportunities and associated risks, take informed decisions and participate actively in the economic growth story of the country by converting saving into investments. Ministry of Corporate Affairs (MCA) has a dedicated approach for empowering investors through education and awareness building.

MCA on 27th September, 2007 launched a website www.iepf.gov.in. It provides information about IEPF and the various activities that have been undertaken/ funded by it. This website provides information on various aspects such as role of capital market, IPO investing, Mutual Fund Investing, Stock Investing, Stock Trading, Depository Account, Debt Market, Derivatives, Indices (comic strip), Index Fund, Investor Grievances & Arbitration (Stock Exchanges), Investor Rights & Obligations, Do's and Don'ts etc.

Ministry of Corporate Affairs has taken various initiatives to educate investors, particularly, since 2001, the Investor Education and Protection Fund (IEPF) has been working for educating the investors and for creating greater awareness about investments in the corporate sector.

IRDA's Initiatives on Financial Education

Insurance Regulatory and Development Authority has taken various initiatives in the area of financial literacy. Awareness programmes have been conducted on television and radio and simple messages about the rights and duties of policyholders, channels available for dispute redressal etc., have been disseminated through television and radio as well as the print media through sustained campaigns in English, Hindi and 11 other Indian languages. IRDA conducts an annual seminar on policy holder protection and welfare and also partially sponsors seminars on insurance by consumer bodies. IRDA has got a pan India survey on awareness levels about insurance carried out through the NCAER in a bid to improve on its strategy of creating insurance awareness. IRDA has also brought out publications of 'Policyholder Handbooks' as well as a comic book series on insurance. A dedicated website for consumer education in insurance is on the verge of launch

IRDA's Integrated Grievance Management System (IGMS) creates a central repository of grievances across the country and provides for various analyses of data indicative of areas of concern to the insurance policyholder.

PFRDA Initiatives on Financial Education

The Pension Fund Regulatory and Development Authority, India's youngest regulator has been engaged in spreading social security messages to the public. PFRDA has developed FAQ on pension related topics on its web, and has been associated with various non government organizations in India in taking the pension services to the disadvantaged community.

PFRDA's initiatives have become more broad-based with direct mass publicity on NPS - both as individual model through POPs and group models through Aggregators. PFRDA has issued advertisements in print media and electronic media through radio and television. PFRDA appointed intermediaries are called Aggregators who are directly responsible for pension awareness mostly in vernacular languages and in line with socio-economic sensibilities.

Market players Initiatives on Financial Education

Commercial banks are increasingly realizing that they are missing out on large segment of financially illiterate and excluded segment of prospective customers. Also, in view of the national emphasis on electronic benefit transfer the commercial banks have initiated various measures for creating awareness through Financial Literacy and Counseling Centers and Rural Self Employment Training Institutes on financial literacy. The objective of these centers is to advise people on gaining access to the financial system including banks, creating awareness

among the public about financial management, counseling people who are struggling to meet their repayment obligations and help them resolve their problems of indebtedness, helping in rehabilitation of borrowers in distress etc. Some of these credit counseling centers even train farmers/women groups to enable them to start their own income generating activities to earn a reasonable livelihood. Even top management of commercial banks is undertaking Outreach visits to villages with a view to spread financial literacy.

Similarly, many Stock Exchanges, Broking Houses and Mutual Funds have initiatives in the field of financial education that spawns conducting of seminars, issuance of do's and don'ts and newspaper campaigns. Insurance companies too, carry out campaigns and other educational activities for generic education in insurance.

INVESTOR GRIEVANCE REDRESSAL MECHANISM AT SEBI

INVESTOR GRIEVANCES

There will be occasions when an investor has a complaint against, a listed company or an intermediary registered with SEBI. In the event of such complaint, the investor should first approach the concerned company/ intermediary against whom there is a complaint. Sometimes the response received may not be satisfactory. Therefore, investors should know as to which authority they should approach, to get their complaints redressed.

SCORES (SEBI COMPLAINTS REDRESS SYSTEM)

SCORES is a web based centralized grievance redress system of SEBI (<http://scores.gov.in>). SCORES enables investors to lodge and follow up their complaints and track the status of redressal of such complaints online from the above website from anywhere. This enables the market intermediaries and listed companies to receive the complaints online from investors, redress such complaints and report redressal online. All the activities starting from lodging of a complaint till its closure by SEBI would be online in an automated environment and the complainant can view the status of his complaint online. An investor, who is not familiar with SCORES or does not have access to SCORES, can lodge complaints in physical form at any of the offices of SEBI. Such complaints would be scanned and also uploaded in SCORES for processing.

The salient features of SCORES are:

- SCORES is web enabled and provides online access 24 x 7;
- Complaints and reminders thereon can be lodged online at the above website at anytime from anywhere;
- An email is generated instantaneously acknowledging the receipt of complaint and allotting a unique complaint registration number to the complainant for future reference and tracking;
- The complaint forwarded online to the entity concerned for its redressal;
- The entity concerned uploads an Action Taken Report (ATR) on the complaint;
- SEBI peruses the ATR and closes the complaint if it is satisfied that the complaint has been redressed adequately;
- The concerned investor can view the status of the complaint online from the above website by logging in the unique complaint registration number;
- The entity concerned and the concerned investor can seek and provide clarification on his complaint online to each other;
- Every complaint has an audit trail; and
- All the complaints are saved in a central database which generates relevant MIS reports to enable SEBI to take appropriate policy decisions and/or remedial actions, if any.

How to lodge complaint in SCORES?

To register a complaint online on SCORES portal, (<http://scores.gov.in>) click on “Complaint Registration” under “Investor Corner”. The complaint registration form contains personal details and complaint details. There are certain mandatory fields in the Form. These fields include Name, Address for correspondence, State, Email Address of Investor. After filling the personal details, select the complaint category, entity name, nature of complaint related to, complaint details in brief (up to 1000 characters). A PDF document (up to 1MB of size for each nature of complaint) can also be attached along with the complaint as the supporting document. On successful submission of complaint, system generated unique registration number will be displayed on the screen which may be noted for future correspondence. An email acknowledging the complaint with complaint registration number will also be sent to the complainant’s email id entered in the complaint registration form.

What are the limitations in dealing with complaints?

To make efficient complaints redressal mechanism through SCORES, it is mandated by SEBI to all stock brokers and DPs that they shall redress the complaints **within 15 days from the date of receipt of complaint**. In case of additional information required from the complainant, then it should be redress **within 7 days** from the date of receipt of complaint, the period of 15 days shall be count from the receipt of additional information.

Sometimes a complaint is successfully resolved and the entity is advised to send reply to complainant. But in certain cases, the entity or company denies wrongdoing, and it remains unclear as to who is wrong or whether any wrongdoing occurred at all. If this happens, SEBI cannot act as a judge or an arbitrator and force the entity or company to resolve the complaint. Further, SEBI cannot act as personal representative or attorney of the complainant. Securities laws and other laws provide important legal rights and remedies if an investor has suffered wrongdoing. On their own, investors can also seek to resolve their complaint through the courts, consumer courts, or arbitration.

When can a case be referred for arbitration?

If the grievance is not resolved by the Stock Exchange/Depository due to disputes, an investor can file arbitration subject to the Bye-laws, Rules and Regulations of the exchange / Depository. All claims, differences or disputes between the investors and stock brokers/depository participants can be filed for arbitration. To obtain information about when and how to file an arbitration claim, please visit:

Bombay Stock Exchange

<http://www.bseindia.com/investors/Research.aspx?expandable=0>

National Stock Exchange

http://www.nseindia.com/content/assist/asst_investser.htm

Central Depository Services Limited

<http://www.cdslindia.com/downloads/Operating%20Instruction/Chapters-as-of-June-2011.pdf>

National Securities Depository Limited

<https://nsdl.co.in>

Simplified arbitration can be a less costly alternative to legal recourse before the courts of law. If the investor has an account with the broker or a depository participant (DP), he/she can choose arbitration to settle disputes. The investor generally cannot pursue an issue through arbitration if it is barred by limitation prescribed. When deciding whether to arbitrate, the investor has to bear in mind that if the broker or DP goes out of business or declares bankruptcy, he/she might not be able to recover money even if the arbitrator or court rules in his/her favor. However, with certain restriction to the nature of transactions, Stock Exchanges may settle on case to case basis the claim of an investor up to a limit prescribed in the “Investor protection fund” guidelines of the respective Stock Exchange.

The claimant is required to carefully review the rules governing simplified arbitration before filing a claim and should also weigh the costs of arbitrating against the likelihood of being able to collect any award in favor. An investor, who has a claim / counter claim upto ₹10 lakh and files arbitration reference for the same within six months, need not make any deposit for filing arbitration.

When can SEBI take action for non resolution of the complaint?

While the entity is directly responsible for redressal of the complaint, SEBI initiates action against recalcitrant entities on the grounds of their unsatisfactory redressal of large number of investor complaints as a whole.

Which are the matters that are not considered as complaints by SEBI?

- Complaints that are incomplete or not specific
- Allegations without supporting documents
- Offering suggestions or seeking guidance/explanation
- Seeking explanation for non-trading of shares or illiquidity of shares
- Not satisfied with trading price of the shares of the companies
- Non-listing of shares of private offer
- Disputes arise out of private agreement with companies/intermediaries.

SEBI (INFORMAL GUIDANCE) SCHEME, 2003

In the interests of better regulation of and orderly development of the Securities market, SEBI has issued SEBI (Informal Guidance) Scheme 2003. The following persons may make a request for informal Guidance under the scheme:

- (a) any intermediary registered with the SEBI.
- (b) any listed company.
- (c) any company which intends to get any of its securities listed and which has filed either a listing application with any stock exchange or a draft offer document with the Board or the Central Listing authority.
- (d) any mutual fund trustee company or asset management company.
- (e) any acquirer or prospective acquirer under the SEBI (Substantial Acquisition of Shares & Takeovers) Regulations, 2011.

The Guidance Scheme, further deals with various aspects such as the nature of request, fees to be accompanied alongwith request letter, disposal of requests, SEBI's discretion not to respond certain types of requests and confidentiality of requests etc.

The informal guidance may be sought for and given in two forms:

- **No action letters:** SEBI indicates that the Department would or would not recommend any action under any Act, Rules, Regulations, Guidelines, Circulars or other legal provisions administered by SEBI to the Board if the proposed transaction described in a request made under para 6 is consummated.
- **Interpretive letters:** SEBI provides an interpretation of a specific provision of any Act, Rules, Regulations, Guidelines, Circulars or other legal provision being administered by SEBI in the context of a proposed transaction in securities or a specific factual situation.

The request seeking informal guidance should state that it is being made under this scheme and also state whether it is a request for a no action letter or an interpretive letter and should be accompanied with a fee of ₹

25,000/- and addressed to the concerned Department of SEBI. It should also describe the request, disclose and analyse all material facts and circumstances involved and mention all applicable legal provisions. SEBI may dispose off the request as early as possible and in any case not later than 60 days after the receipt of the request. The Department may give a hearing or conduct an interview if it feels necessary to do so. The requestor shall be entitled only to the reply. The internal records or views of SEBI shall be confidential.

SEBI may not respond to the following types of requests:

- (a) those which are general and those which do not completely and sufficiently describe the factual situation;
- (b) those which involve hypothetical situations;
- (c) those requests in which the requestor has no direct or proximate interest;
- (d) where the applicable legal provisions are not cited;
- (e) where a no action or interpretive letter has already been issued by that or any other department on a substantially similar question involving substantially similar facts, as that to which the request relates;
- (f) those cases in which investigation, enquiry or other enforcement action has already been initiated;
- (g) those cases where connected issues are pending before any Tribunal or Court and on issues which are subjudice; and,
- (h) those cases where policy concerns require that the Department does not respond.

Where a request is rejected for non-compliance, the fee if any paid by the requestor shall be refunded to him after deducting therefrom a sum of ₹ 5,000/- towards processing charges. However SEBI is not be under any obligation to respond to a request for guidance made under this scheme, and shall not be liable to disclose the reasons for declining to reply the request.

Confidentiality of Request

Any person submitting a letter or written communication under this scheme may request that it receive confidential treatment for a specified period of time not exceeding 90 days from the date of the Department's response. The request shall include a statement of the basis for confidential treatment. If the Department determines to grant the request, the letter or written communication will not be available to the public until the expiration of the specified period. If it appears to the Department that the request for confidential treatment should be denied, the requestor will be so advised and such person may withdraw the letter or written communication within 30 days of receipt of the advise, in which case the fee, if any, paid by him would be refunded to him. In case a request has been withdrawn under clause (c), no response will be given and the letter or written communication will remain with the SEBI but will not be made available to the public. If the letter or written communication is not withdrawn, it shall be available to the public together with any written staff response.

A no action letter or an interpretive letter issued by a Department constitutes the view of the Department but will not be binding on SEBI, though the SEBI may generally act in accordance with such a letter. The letter issued by a Department under this scheme should not be construed as a conclusive decision or determination of any question of law or fact by SEBI. Such a letter cannot be construed as an order of SEBI under Section 15T of the Act and shall not be appealable. Where a no action letter is issued by a Department affirmatively, it means that the Department will not recommend enforcement action to the Board, subject to other provisions of this scheme.

LESSON ROUND UP

- In order to afford adequate protection to the investors, provisions have been incorporated in different legislations such as the Companies Act, 2013, Securities Contracts (Regulation) Act, 1956, Depositories

Act, 1996, and Listing Agreement of the Stock Exchanges supplemented by many guidelines, circulars and press notes issued by the Ministry of Finance, Ministry of Corporate Affairs and SEBI from time to time.

- Investor Education and Protection Fund (IEPF) has been established under Section 125 of the Companies Act, 2013, for promotion of investors' awareness and protection of the interests of investors.
- Investor Education and Protection Fund Authority Rules, 2014 (IEPF Rules) stipulate the activities related to investors' education, awareness and protection for which the financial sanction can be provided under IEPF.
- SEBI issued SEBI (Investor Protection and Education Fund) Regulations, 2009 to protect the interest of investors and provide for the utilization of the fund established under these regulations.
- In the developing countries, the growing number of investors, technically advanced financial markets, liberalised economy etc., necessitates imparting of financial education for better operation of markets and economy and in the interest of investor.
- Ministry of Corporate Affairs (MCA) has taken various initiatives to educate investors, particularly, since 2001, the Investor Education and Protection Fund (IEPF) has been working for educating the investors and for creating greater awareness about investments in the corporate sector.
- MCA launched a website www.iepf.gov.in which provides information about IEPF, various activities that have been undertaken/ funded by it. It also fulfils the need for an information resource for small investors on all aspects of the financial markets and would attempt to do it in the small investors' language.
- SEBI has also launched a comprehensive securities market awareness campaign for educating investors through workshops, audio-visual clippings, distribution of educative investor materials/booklets, dedicated investor website etc.
- SCORES is a web based centralized grievance redress system of SEBI which enables investors to lodge and follow up their complaints and track the status of redressal of such complaints online from the above website from anywhere.
- SEBI (Informal Guidance) Scheme, 2003 deals with various aspects such as the nature of request fees to be accompanied along with letter disposal of requests, SEBI discretion not request and certain types of request and confidentiality of requests, etc.

GLOSSARY

Forward Markets Commission

The Forward Markets Commission (FMC) is a regulatory authority that is overseen by the Ministry of Consumer Affairs, Food and Public Distribution, Government of India. It is a statutory body set up in 1953 under the Forward Contracts (Regulation) Act, 1952.

IPF

Investor Protection Fund is the fund set up by the stock exchanges to meet the legitimate investment claims of the clients of the defaulting members that are not of speculative nature.

Indian Penal Code (IPC)

It is the main criminal code of India. It is a comprehensive code, intended to cover all substantive aspects of criminal law.

Nidhi company

It is a company registered under Companies Act and notified as a nidhi company

by Central Government under Section 406 of Companies Act, 2013. It is a non-banking finance company doing the business of lending and borrowing with its members or shareholders.

SELF TEST QUESTIONS

(These are meant for recapitulation only. Answer to these questions are not to be submitted for evaluation.)

1. Explain the investors rights and responsibilities as an individual shareholder and as a group.
2. Outline the various statutory measures initiated by MCA for investor protection.
3. What is SCORES? Briefly discuss the salient features of SCORES.
4. Explain the utilisations of Investor Protection and Education Fund established under the SEBI (Investor Protection and Education Fund) Regulations, 2009.
5. Who are eligible to make a request under the SEBI (Informal Guidances) Scheme, 2003?

This image shows a blank sheet of white paper with horizontal ruling lines. At the top, there is a solid black rectangular header bar. Below it, the page contains approximately 20 evenly spaced horizontal grey lines, typical of notebook paper. The lines extend across the entire width of the page.

EXECUTIVE PROGRAMME

CAPITAL MARKETS AND SECURITIES LAWS**EP-CM&SL****TEST PAPERS****A Guide to CS Students**

To enable the students in achieving their goal to become successful professionals, Institute has prepared a booklet 'A Guide to CS Students' providing the subject specific guidance on different papers and subjects contained in the ICSI curriculum. The booklet is available on ICSI website and students may download from <http://www.icsi.edu/Portals/0/AGUIDETOCSSSTUDENTS.pdf>

WARNING

It is brought to the notice of all students that use of any malpractice in Examination is misconduct as provided in the explanation to Regulation 27 and accordingly the registration of such students is liable to be cancelled or terminated. The text of regulation 27 is reproduced below for information:

"27. Suspension and cancellation of examination results or registration

In the event of any misconduct by a registered student or a candidate enrolled for any examination conducted by the Institute, the Council or the Committee concerned may suo motu or on receipt of a complaint, if it is satisfied that, the misconduct is proved after such investigation as it may deem necessary and after giving such student or candidate an opportunity to state his case, suspend or debar the person from appearing in any one or more examinations, cancel his examination result, or studentship registration, or debar him from future registration as a student, as the case may be.

Explanation - Misconduct for the purpose of this regulation shall mean and include behaviour in a disorderly manner in relation to the Institute or in or near an Examination premises/centre, breach of any regulation, condition, guideline or direction laid down by the Institute, malpractices with regard to postal or oral tuition or resorting to or attempting to resort to unfair means in connection with the writing of any examination conducted by the Institute".

EXECUTIVE PROGRAMME

CAPITAL MARKETS AND SECURITIES LAWS**TEST PAPER**

(This Test Paper is for recapitulate and practice for the students. Students need not to submit responses/answers to this test paper to the Institute.)

Time Allowed : 3 Hours

Maximum Marks : 100

PART A (60 MARKS)**(CAPITAL MARKETS)****Question No. 1**

- (a) Enumerate the key features of depository system in India. (5 marks)
- (b) Explain the role of Capital Markets in promoting and sustaining the growth of an economy. (5 marks)
- (c) What do you mean by 'Tracking Stock'? State the advantages and disadvantages of Tracking Stock. (5 marks)

Attempt either Question No. 2 or 2A**Question No. 2**

- (a) Briefly explain the disclosures required to be made by a Credit Rating Agency (CRA) under the guidelines issued by SEBI for CRAs. (5 marks)
- (b) What are the eligibility criteria for approval of REITs? (5 marks)
- (c) Explain the process of factoring. (5 marks)

OR**Question No.2A**

What do you mean by Green Debt Securities? Explain the obligations of a Listed Entity which has listed its green debt securities on a recognized stock exchange?

(15 marks)

Question No. 3

- (i) Distinguish between the following:
 - (a) 'Income Oriented Schemes' and 'Growth Oriented Schemes'
 - (b) 'Book Closure and Record Date'
 - (c) 'Deep Discount Bond' and 'Disaster Bonds' (3 marks each)
- (ii) Write short notes on the following:
 - (a) Sponsored ADR/GDR issue
 - (b) Eligible Infrastructure Project
 - (c) Capital Protection Oriented Schemes (2 marks each)

Question No. 4

- (a) Discuss the provisions of Conversion of ECB into equity as per guidelines of RBI. (5 marks)
- (b) Explain the various conditions to be fulfilled by a company to make a private placement of non-convertible redeemable preference shares under SEBI (Issue and Listing of Non Convertible Redeemable Preference Shares) Regulations, 2013. (5 marks)
- (c) What are Offshore Derivative Instruments (ODIs)? Explain the various conditions for Issuance of ODI under the SEBI (Foreign Portfolio Investors) Regulations, 2014? (5 marks)

PART-B (40 marks)**(Securities Laws)****Question No. 5**

- (a) State the provisions relating to Corporatization and Demutualization of Stock Exchanges? (5 marks)
- (b) Discuss the various powers and functions of the SEBI. (7 marks)
- (c) Briefly explain the guidelines issued by SEBI with respect to single registration of depository participants under the SEBI (Depositories and Participants) Regulations, 1996. (8 marks)

Attempt all parts of either Question No. 6 or Question No 6A

Question No.6

- (a) Explain the procedure for delisting of equity shares in case of no exit opportunity given to the public shareholders under SEBI (Delisting of Equity Shares) Regulations, 2009. (5 marks)
- (b) What are the half yearly compliances and annual compliances mentioned under the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 to be complied by a company who has listed its specified securities on a recognized stock exchange? (5 marks)
- (c) What is Institutional Placement Programme (IPP)? Briefly explain the restrictions on making IPP. (10 marks)

OR

Question No.6 A

- (a) What are the exemptions for registration of an Investment Advisers under SEBI (Investment Advisers) Regulations, 2013? (5 marks)
- (b) Discuss the various provisions relating to communication or procurement of Unpublished Price Sensitive Information (UPSI) as enumerated under SEBI (Prohibition of Insider Trading) Regulation, 2015. (5 marks)
- (c) State the threshold and conditions for making the voluntary open offer under SEBI (Substantial acquisition of Shares and Takeovers) Regulation, 2011. (5 marks)
- (d) Explain the provisions relating to the utilizations of Investor Education and Protection Fund established under the Companies Act, 2013. (5 marks)
