PART ONE: POLICIES AND PROGRAMMES

The Annual Report of the Securities and Exchange Board of India (SEBI) for 2006-07 articulates the policies and programmes of SEBI and its working and operations during the financial year as per format prescribed by the Securities and Exchange Board of India (Annual Report) Rules, 1994. SEBI is committed to achieve the three statutory objectives, namely: (a) protection of the interests of investors in securities; (b) development of the securities market and (c) regulation of the securities market.

Keeping in line with these objectives, this Report elucidates the manner in which SEBI discharged its responsibilities and exercised its powers during the year in terms of: (a) the Securities and Exchange Board of India Act, 1992; (b) the Securities Contracts (Regulation) Act, 1956; (c) the Depositories Act, 1996 and (d) certain provisions of the Companies Act, 1956. The Report also provides a description of the developments in the Indian securities market during 2006-07, in the context of changing dynamics of the market regulations as implemented by SEBI.

On the backdrop of an ever increasing integration of global financial markets, SEBI continued its efforts to come out with regulations to meet the challenges posed by domestic and global developments. SEBI in its attempt to strengthen the regulatory framework reviewed existing policies and programmes, introduced new guidelines and regulations to promote orderly growth of securities market while ensuring its transparency, efficiency, fairness, safety, and integrity. Major initiatives and developments in the securities market during 2006-07 are presented below (Box 1.1).

Box 1.1: Major Initiatives and Developments in the Securities Market

I. Primary Securities Market

❖ ***Continuous Listing Requirement: Minimum Level of Public Shareholding***

To enable a minimum level of public shareholding, listed companies will now be required to maintain minimum level of public shareholding at 25 per cent of the total shares issued for continued listing on stock exchanges. Exemptions are provided to companies which are required to maintain at least 10 per cent but less than 25 per cent in accordance with the Rule 19 (2) (b) of the Securities Contracts (Regulation) Rules, 1957 and to companies that have two crore or more number of listed shares, and market capitalisation of Rs. 1,000 crore or more.

❖ ***Optional IPO Grading***

SEBI framed Guidelines relating to disclosure of grading of the Initial Public Offer (IPO) by issuer companies who may want to opt for grading of their IPOs by the rating agencies. If the issuer companies opt for grading, then they are required to disclose the grades, including the unaccepted ones, in the prospectus.

❖ ***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.

Box 1.1: Major Initiatives and Developments in the Securities Market

I. *Primary Securities Market* (Contd.)

❖ ***Qualified Institutions' Placement (QIP)***

SEBI issued directions for the issuing companies, relating to Qualified Institutions' Placement, to pave the path for a fast and cost-effective way of raising resources from Indian securities market.

❖ ***Corporate Bond Market – Launch of Reporting Platform***

SEBI directed, both BSE and NSE, to introduce a trade reporting platform for corporate bonds.

❖ ***Common Platform for Electronic Filing and Dissemination of Information Relating to Listed Companies***

At the instance of SEBI, BSE and NSE jointly launched a common portal www.corpfiling.co.in on January 01, 2007, for dissemination of filings made by companies listed on these exchanges, in terms of the listing agreement.

II. *Secondary Securities Market*

❖ ***Value at Risk (VaR) Margining in Cash Market***

It was decided to update the applicable VaR margins in the cash market at least five times in a day instead of only at the end of the trading day and then apply it to the open positions for the subsequent trading day, as practised in the derivatives market.

❖ ***Mandatory Requirement of PAN for Trading in the Cash Market***

In order to further strengthen Know Your Client (KYC) norms in the cash market and to generate a reliable audit trail, PAN was made mandatory for all transactions in the cash market with effect from January 01, 2007.

❖ ***Mandatory Requirement of PAN for Opening and Operating Demat Accounts***

PAN was made mandatory for all demat accounts, opened after April 01, 2006, pertaining to all categories including minors, trusts, foreign corporate bodies, banks, corporates, FIIs, and NRIs. For demat accounts that existed prior to April 01, 2006, time for furnishing and verification of PAN card details was extended upto December 31, 2006.

❖ ***Standing Committee for Addressing Problems in Computerised Trading***

The stock exchanges were advised to set up Standing Committees to investigate the problems in computerised trading system, such as, hanging, slowdown, breakdown, and any other problem. The matter would be referred to respective Standing Committee, even if, the duration of disruption is less than five minutes.

❖ ***Dissemination of Tariff/Charge Structure of Depository Participants (DPs)***

Following the representations made by investors, on different charge/tariff structure of various DPs, it was decided that the DPs will immediately inform respective depositories, about any change in charge/tariff structure. The depositories were directed to display charge/tariff structure of various DPs on their websites to help investors in taking informed decisions.

Box 1.1: Major Initiatives and Developments in the Securities Market

II. Secondary Securities Market *(Contd.)*

❖ ***Safeguards to Address the Transfer of Securities of the Investors***

A large number of representations were received from investors relating to transfer of securities from Beneficiary Owners' (BOs) Account without proper authorisation. Accordingly, the DPs were instructed to put in place adequate safeguards.

❖ ***Policy Initiatives for Derivatives***

Procedure for re-introduction of derivatives contracts and modified position limits were reviewed by the Secondary Market Advisory Committee (SMAC). Further, based on a decision taken by SEBI Board, Derivatives Market Review Committee was set up to carry out a comprehensive review of developments and to suggest future directions for derivatives market in India.

❖ ***Corporatisation and Demutualisation (C & D) of Stock Exchanges***

SEBI notified Securities Contracts (Regulation) (Manner of Increasing and Maintaining Public Shareholding in Recognised Stock Exchanges), Regulation, 2006 on November 13, 2006, whereby the recognised stock exchanges were directed to ensure that at least 51 per cent of its equity share capital is held by public, either by fresh issue of equity shares to the public, through issue of prospectus or through (i) offer for sale, (ii) placement of shares to institutions, (iii) issue of equity shares on private placement, and (iv) any combination of the above.

III. Mutual Funds

❖ ***Rationalisation of Initial Issue Expenses and Dividend Distribution Procedures***

To contain frequent churning in mutual fund schemes, close-ended schemes were permitted to charge initial issue expenses to the scheme while open-ended schemes can charge only entry load for the purpose of meeting the expenses connected with sales and distribution of schemes. Dividend distribution procedures were also specified by SEBI. Notice to be issued to public within one calendar day of the decision by the trustees on dividend distribution.

❖ ***Undertaking from Trustees for New Scheme Offer Document***

To address concerns regarding launch of similar products, mutual fund trustees were directed to certify that the scheme approved by them is a new product and it is not a minor modification of existing scheme/product.

❖ ***Investment in ADRs/GDRs/Foreign Securities and Overseas Exchange Traded Funds (ETFs)***

Following the Finance Bill 2006-07 and subsequent raising of limit by RBI, the maximum ceiling for individual mutual funds to invest in ADRs/GDRs issued by Indian companies, equity of overseas companies listed on recognised stock exchanges overseas and rated debt securities was raised from USD 50 million to USD 100 million. Subsequently, the limit was further raised to USD 150 million. Mutual funds were also advised to appoint a dedicated fund manager for making such investments.

Box 1.1: Major Initiatives and Developments in the Securities Market

III. Mutual Funds *(Contd.)*

❖ ***Introduction of Capital Protection Oriented Schemes***

SEBI (Mutual Funds) Regulations, 1996 were amended to permit launch of Capital Protection Oriented schemes.

❖ ***Uniform Cut-off Timing for Applicability of Net Asset Value (NAV)***

Following the various systemic changes made by RBI in money market the cut-off timings for applicability of NAV, in case of purchases and redemptions of liquid schemes, were revised.

❖ ***Dispatch of Statement of Accounts***

SEBI directed mutual funds to dispatch the statement of accounts to the unit holders under Systematic Investment Plan (SIP) / Systematic Transfer Plan (STP) / Systematic Withdrawal Plan (SWP) once every quarter ending March, June, September and December, within 10 working days of the end of the respective quarter. SEBI also advised mutual funds to provide statement of accounts to the unit holders, who have not transacted during the last six months, to ensure better information dissemination.

❖ ***Launch of Gold Exchange Traded Funds (GETFs)***

SEBI amended SEBI (Mutual Funds) Regulations, 1996 to specify the methodology for valuation of gold for the purpose of GETFs. Accordingly, the gold held by a GETF scheme shall be valued at the AM fixing price of London Bullion Market Association (LBMA) in US dollars per troy ounce for gold having a fineness of 995.0 parts per thousand, subject to prescribed adjustments. Two GETF schemes were launched during the year, offering investors better diversification opportunity.

❖ ***Real Estate Mutual Fund***

SEBI Board approved the draft guidelines for Real Estate Mutual Funds (REMFs). REMF means a scheme of a mutual fund which has investment objective to invest directly or indirectly in real estate property and shall be governed by the provisions and guidelines under SEBI (Mutual Funds) Regulations.

IV. Foreign Institutional Investors (FIIs)

❖ ***Investment in Debt Securities***

The investment limit for FIIs in Government Securities (including Treasury Bills) was raised from USD 2 billion to USD 2.6 billion by RBI. The list of eligible investment categories of FIIs was enlarged to allow more participation in Indian securities market.

V. Regulatory Developments

❖ *The following rules were rescinded during 2006-07:*

- *SEBI Intermediary Rules (Stock Brokers and Sub-brokers, 1992; Merchant Bankers, 1992; Underwriters, 1993; Portfolio Managers, 1993; Debenture Trustees, 1993; Registrars to an Issue and Share Transfer Agents, 1993 and Bankers to an Issue, 1994).*

Box 1.1: Major Initiatives and Developments in the Securities Market

*V. **Regulatory Developments** (Contd.)*

- *Amendment to SEBI (Procedure for Holding Inquiry and Imposing Penalty by Adjudicating Officer) Amendment Rules, 1995, to provide for appointment of presenting officer by SEBI in adjudication proceedings.*

❖ *The following Regulations were framed during 2006-07:*

- *SC(R) (Manner of Increasing and Maintaining Public Shareholding in Recognised Stock Exchanges) Regulations, 2006*
- *SEBI (Regulatory Fee on Stock Exchanges) Regulations, 2006*

❖ *The following Regulations were amended during 2006-07:*

- *SEBI (Stock Brokers and Sub-brokers) Regulations, 1992*
- *SEBI (Merchant Bankers) Regulations, 1992*
- *SEBI (Portfolio Managers) Regulations, 1993*
- *SEBI (Registrars to an Issue and Share Transfer Agents) Regulations, 1993*
- *SEBI (Underwriters) Regulations, 1993*
- *SEBI (Debenture Trustees) Regulations, 1993*
- *SEBI (Bankers to an Issue) Regulations, 1994*
- *SEBI (Foreign Institutional Investors) Regulations, 1995*
- *SEBI (Custodian of Securities) Regulations, 1996*
- *SEBI (Venture Capital Funds) Regulations, 1996*
- *SEBI (Mutual Funds) Regulations, 1996*
- *SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997*
- *SEBI (Buy Back of Securities) Regulations, 1998*
- *SEBI (Credit Rating Agencies) Regulations, 1999*
- *SEBI (Foreign Venture Capital Investors) Regulations, 2000*
- *SEBI (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002*
- *SEBI (Ombudsman) Regulations, 2003*
- *SEBI (Central Listing Authority) Regulations, 2003*

1. GENERAL MACRO-ECONOMIC ENVIRONMENT

India continued to maintain its pre-eminence as one of the fastest growing economies of the world. The Indian economy remained firm during 2006-07, mainly driven by continued growth in industry and services sectors. According to advance estimates of Central Statistical Organisation (CSO), real GDP at factor cost at 1999-00 prices (New Series) grew by 9.4 per cent in 2006-07 on top of 9.0 per cent (quick estimates) achieved in the previous year (Table 1.1). The industrial sector performed well (11.0 per cent), mainly led by manufacturing activities which recorded a growth of 12.3 per cent in 2006-07 compared to 9.1 per cent in 2005-06 (Table 1.2). The services sector continued to be the main driver of growth in India with double digit growth (11.0 per cent) for the

Table 1.1: National Income (at 1999-00 prices)

(Rs. crore)

Item	2004-05	2005-06 (Quick Estimates)	2006-07 (Revised Estimates)
1	2	3	4
A. Estimates at Aggregate Level			
1. National Product			
1.1 Gross National Product (GNP) at factor cost	23,67,711	25,80,761 (9.0)	28,29,349 (9.6)
1.2 Net National Product (NDP) at factor cost	21,03,350	22,95,243 (9.1)	25,22,576 (9.9)
2. Domestic Product			
2.1 Gross Domestic Product (GDP) at factor cost	23,89,660	26,04,532 (9.0)	28,48,157 (9.4)
2.2 Net Domestic Product (NDP) at factor cost	21,25,299	23,19,014 (9.1)	25,41,384 (9.6)
B. Estimates at Per Capita Level			
1. Population (million)	1,090	1,107 (1.6)	1,122 (1.4)
2. Per Capita NNP at factor cost (Rs.)	19,297	20,734 (7.4)	22,483 (8.4)

Note: Figures in the parentheses are percentage change over the previous year.

Source: Central Statistical Organisation.

Table 1.2: GDP (at Factor Cost) by Economic Activity (at 1999-00 prices)

(Rs. crore)

Industry	2004-05	2005-06 (Quick Estimates)	2006-07 (Revised Estimates)	Percentage Change over Previous Year	
				2005-06	2006-07
1	2	3	4	5	6
1. Agriculture, Forestry & Fishing	4,83,080	5,12,147	5,25,875	6.0	2.7
2. Mining & Quarrying	52,250	54,128	56,912	3.6	5.1
3. Manufacturing	3,61,115	3,93,956	4,42,503	9.1	12.3
4. Electricity, Gas & Water Supply	54,531	57,401	61,671	5.3	7.4
5. Construction	1,55,431	1,77,543	1,96,555	14.2	10.7
6. Trade, Hotels, Transport and Communication	6,16,024	6,80,237	7,68,578	10.4	13.0
7. Financing, Insurance, Real Estate & Business Services	3,23,187	3,58,535	3,96,394	10.9	10.6
8. Community, Social & Personal Services	3,44,042	3,70,584	3,99,668	7.7	7.8
GDP at Factor Cost	**23,89,660**	**26,04,532**	**28,48,157**	**9.0**	**9.4**

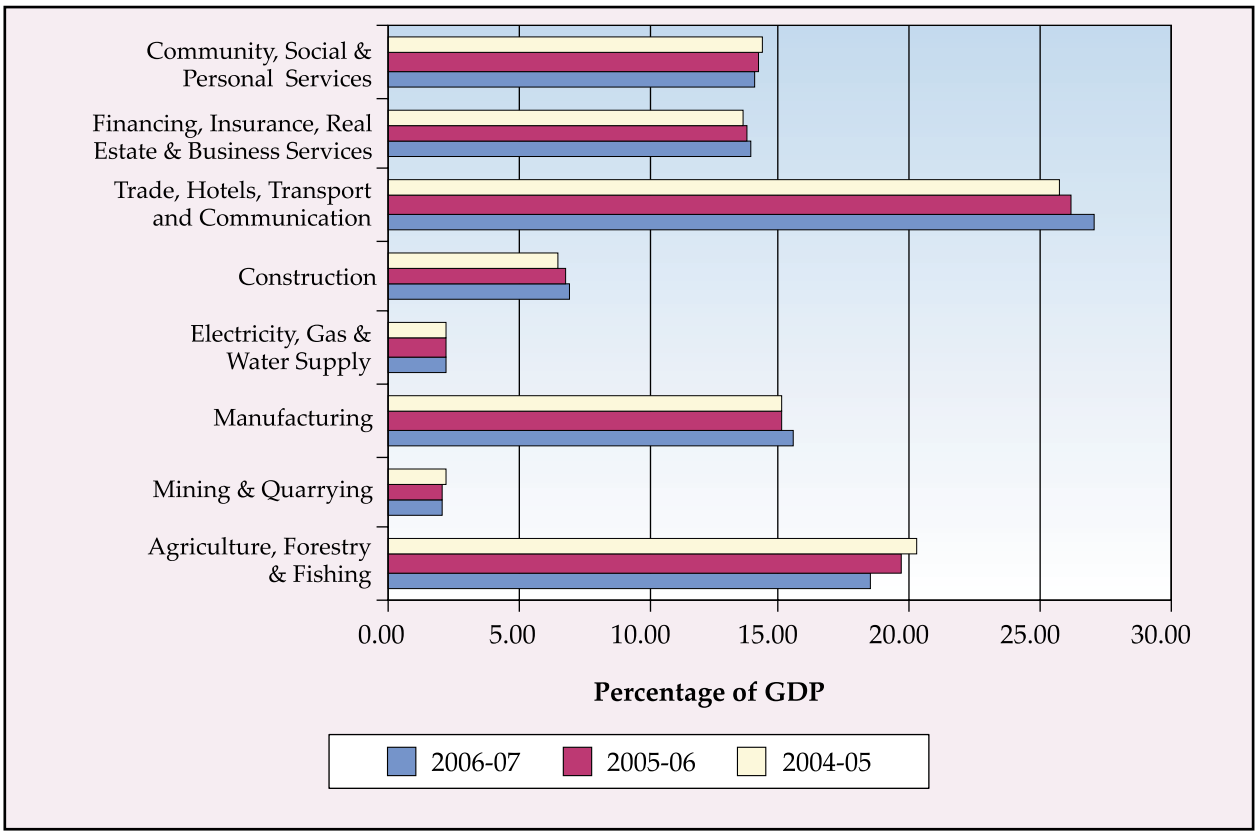
Source: Central Statistical Organisation.

third year in succession. Following a tepid South-West monsoon and an average North-East monsoon, the agricultural sector clocked a growth of 2.7 per cent in 2006-07 as against 6.0 per cent in 2005-06. This was reflected in the fact that the share of 'agriculture and allied activities' in the overall GDP declined from 19.7 cent in 2005-06 to 18.5 per cent in 2006-07 (Chart 1.1). In contrast, the share of services sector improved from 60.9 per cent to 61.9 per cent and that of industry increased from 19.4 per cent to 19.7 per cent, during the same period. During the Tenth Plan (2002-07) period, India's real GDP grew at an average rate of more than 7.6 per cent compared to 5.5 per cent in the Ninth Plan period (1997-2002).

Major factors contributing to acceleration in the manufacturing activities were buoyant exports, increase in domestic demand, rise in capacity utilisation, encouraging outlook on business expectations, congenial investment climate etc. Along with investment growth, capital goods and consumer goods sectors performed well. 'Textile products', 'beverages, tobacco and related products', 'basic metals and alloy industries' and 'transport equipment and parts' witnessed double digit growth in 2006-07. However, growth in the intermediate goods and infrastructure sector was sluggish. According to business expectations surveys, conducted by various agencies, India's industrial sector is likely to continue its strong performance in the near future.

Services sector continued to remain the largest contributor to overall GDP growth. Within the services sector, 'construction', 'trade, hotel, transport and communication' maintained double digit growth in 2006-07. Community, social and personal services grew marginally during 2006-07.

Chart 1.1: Share of Components of GDP (at Factor Cost)



Latest data on India's savings and investments are available upto 2005-06. According to CSO, India's Gross Domestic Savings (GDS) as proportion of GDP at current market prices (New Series) increased from 31.1 per cent in 2004-05 to 32.4 per cent in 2005-06. Public sector savings declined from 2.4 per cent in 2004-05 to 2.0 per cent in 2005-06 mainly on account of decrease in savings of public authorities. Private corporate sector savings improved moderately from 7.2 per cent in 2004-05 to 8.1 per cent in 2005-06, on the back of robust corporate profits. Savings of household sector increased by 0.8 per cent to 22.4 per cent in 2005-06 after witnessing a decline in the same period during 2004-05. Household savings in the form of financial assets increased while it decreased for physical assets. The Gross Domestic Capital Formation (overall investment), exceeded GDS by 1.4 per cent to 33.8 per cent of GDP in 2005-06 reflecting net inflow of foreign savings (Table 1.3).

'Deposits' continued to dominate as a major component of the gross financial savings by the households. The share of deposits in total financial savings increased from 37.0 per cent in 2004-05 to 47.4 per cent

Table 1.3: Gross Domestic Savings and Investment

Item	Amount in Rupees Crore				Per cent of GDP at current market prices			
	2002-03	2003-04	2004-05@	2005-06*	2002-03	2003-04	2004-05@	2005-06*
1	2	3	4	5	6	7	8	9
1. Household Sector Savings	5,59,074	6,57,327	6,74,834	7,97,117	22.74	23.77	21.58	22.35
a) Financial Assets	2,53,255	3,13,260	3,18,791	4,16,462	10.30	11.33	10.20	11.67
b) Physical Assets	3,05,819	3,44,067	3,56,043	3,80,655	12.44	12.44	11.39	10.67
2. Private Corporate Sector Savings	1,03,965	1,31,355	2,23,512	2,88,430	4.23	4.75	7.15	8.09
3. Public Sector Savings	-14,057	31,822	74,682	71,262	-0.57	1.15	2.39	2.00
4. Gross Domestic Savings (GDS)	6,48,982	8,20,504	9,73,028	11,56,809	26.40	29.67	31.12	32.43
5. Net Capital Inflow (+)/ Outflow (-)	-28,486	-45,380	13,338	47,665	-1.16	-1.64	0.43	1.34
6. Gross Domestic Capital Formation (GDCF)	6,20,496	7,75,125	9,86,366	12,04,474	25.24	28.03	31.55	33.77
7. Final Consumption Expenditure	18,36,446	20,24,085	22,16,271	24,76,590	74.71	73.19	70.88	69.43
a) Private Final Consumption Expenditure	15,45,126	17,13,450	18,73,729	20,72,079	62.86	61.96	59.93	58.09
b) Government Final Consumption Expenditure	2,91,320	3,10,635	3,42,542	4,04,511	11.85	11.23	10.96	11.34
Memo Items								
Savings Investment Balance (4-6)	28,486	45,379	-13,337	-47,665	1.16	1.64	-0.43	-1.34
Public Sector Balance#	-1,63,381	-1,42,775	-1,45,805	-1,93,164	-6.65	-5.16	-4.66	-5.42
Private Sector Balance#	2,11,640	2,53,265	2,32,258	2,45,176	8.61	9.16	7.43	6.87
a) Private Corporate Sector	-41,615	-59,995	-86,533	-1,71,286	-1.69	-2.17	-2.77	-4.80
b) Household Sector	2,53,255	3,13,260	3,18,791	4,16,462	10.30	11.33	10.20	11.67
Investment in Shares and Debenture	5,504	492	4,967	29,008	0.22	0.02	0.16	0.81

@ : Provisional Estimates. * : Quick Estimates. # : Investment figures are not adjusted for errors and omissions.

Source: Central Statistical Organisation, Reserve Bank of India.

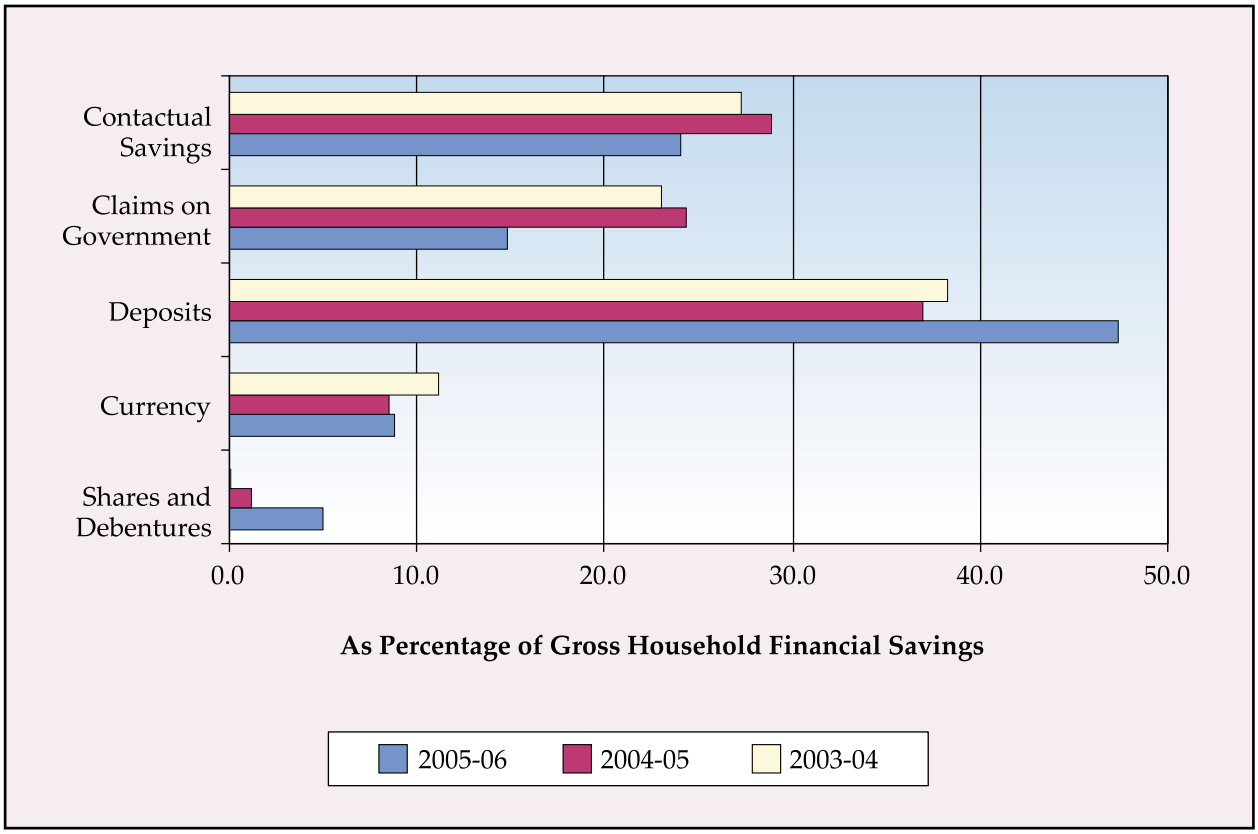
in 2005-06 (Chart 1.2). On the contrary, households' claims on Government declined substantially from 24.4 per cent in 2004-05 to 14.7 per cent in 2005-06. Thus, there was a visible shift in the pattern of household financial savings from claims on Government to deposits due to higher returns available to them from various types of fixed deposits offered by banks and equity investments.

During 2005-06, other major components of financial savings were contractual savings, mainly insurance (14.2 per cent), followed by provident and pension funds (10 per cent) and currency (8.8 per cent). Investment in shares and debentures by the households as a proportion of gross total financial savings increased significantly from 1.1 per cent in 2004-05 to 4.9 per cent in 2005-06. Shares and debentures as proportion to GDP (at current market prices) improved significantly from 0.2 per cent to 0.8 per cent during the same period.

Lending activities by commercial banks further accelerated during 2006-07. For the third year in succession, the non-food credit witnessed expansion reflecting pick-up in GDP growth, in general and industrial activities, in particular. Credit to services sector also accelerated during 2006-07, including retail lending, particularly to personal loan and housing sector. In consonance with the high GDP growth, there was a sizeable credit pick-up in respect of petroleum, basic metals and metal products, textiles, food processing, infrastructure, engineering and chemicals. During 2006-07, credit growth outpaced the deposit growth. The liquidity condition remained tight during the greater part of the year following monetary tightening and imposition of strict provisioning norms by Reserve Bank of India (RBI).

Amidst a rally in stock prices, financial markets remained, by and large, stable

Chart 1.2: Share of Types of Savings in Financial Savings of the Household Sector



during the year under review, except for the month of May 2006 and February 2007, when corrections took place in stock market.

High credit demand coupled with inadequate growth in deposits, exerted pressure on interest rates, particularly at the short-end of the market. As a result, the yield curve flattened reducing the spread between short and long yields. Corporates restructured their debt profile and also resorted to external commercial borrowings (ECBs). Moreover, they mobilised sizeable amount of resources through the issue of ADRs and GDRs in addition to accessing the domestic markets through a number of public issues, rights issues, and private placements.

Inflation on a point to point basis, measured by variation in the Wholesale Price Index (WPI), was 5.7 per cent at the end of March 2007 compared to 4.1 per cent a year ago. On an average basis, the inflation rate was 5.4 per cent in 2006-07 compared to 4.4 per cent in the previous year. Prices of manufactured products (weight: 63.8 per cent in WPI) rose by 5.8 per cent compared to 1.9 per cent a year ago. Following the softening of international crude oil prices, fuel group recorded a rise of 1.0 per cent in 2006-07 which was lower than that of 8.3 per cent in the previous year. As a part of deliberate policy, in order to contain the inflation, the Union Government did not pass on the entire burden of rise in international crude oil prices to the consumers.

India's import bill increased significantly during 2006-07. The major share was contributed by oil. The non-oil imports also rose due to high growth rates and buoyancy in the industrial activities. As a result, trade deficit widened during 2006-07. Bulk of trade deficit was financed through net receipts under invisibles, particularly through remittances from the Indian migrant workers abroad and earnings from exports of IT-enabled services. The capital flows, which more than offset the current account deficit, contributed to the accumulation of foreign exchange reserves of RBI. India's foreign exchange reserves rose by USD 47.6 billion during 2006-07, on account of rising inflow of foreign direct investment (FDI) and external commercial borrowings by Indian companies overseas.

2. REVIEW OF POLICIES AND PROGRAMMES

SEBI initiated a number of policies during 2006-07 in consultation with the Government of India. These policies and programmes are presented in this section under six major heads *viz.* primary securities market, secondary securities market, mutual funds, foreign institutional investors, corporate restructuring and investor awareness and investor protection. The section is concluded with 'retrospect and prospects'.

I. Primary Securities Market

A developed primary market is crucial for resource mobilisation by companies to raise funds for expansion and growth plans. Indian primary market, which witnessed an increased activity in 2005-06, showed further strength in 2006-07. The ongoing reforms in the primary market improved the confidence of the investors as well as the issuers. A number of companies entered the primary market for resource mobilisation. Response of various categories of investors to public issues was encouraging. A detailed discussion on number of issues, amount mobilised, size and composition of issues and industry-wise resource mobilised is given in the Part Two of this report. Major policy initiatives taken by SEBI during 2006-07 relating to the primary market are:

i. Continuous Listing Requirement: Minimum Level of Public Shareholding

As a pre-condition to maintain continuous listing, now listed companies are

required to maintain a minimum level of public shareholding at 25 per cent of the total shares issued. The exception being companies which are required to maintain more than 10 per cent but less than 25 per cent in accordance with the Rule 19 (2) (b) of the Securities Contracts (Regulation) Rules, 1957 as well as the companies, that have two crores or more number of listed shares and Rs. 1,000 crore or more of market capitalisation.

SEBI provided for a transparent mechanism to graduate to compliance of the continuous listing requirements for companies which are currently non-compliant companies or companies which might become non-compliant in future.

Correspondingly, SEBI provided for a revised format for shareholding pattern to be disclosed in accordance with Clause 35 of the equity listing agreement. In the revised format, shareholding pattern will be indicated under three categories, viz. 'shares held by promoter and promoter group', 'shares held by public' and 'shares held by custodians and against which depository receipts have been issued.'

ii. Optional IPO Grading

SEBI prescribed Guidelines relating to grading of the IPO by issuer company who may want to opt for grading of their IPO by the rating agencies. These Guidelines are recommendatory in nature. As per the Guidelines, the issuers are required to state on the cover page of the offer document whether they have opted for an IPO grading. In case, the issuer company opts for a grading, then these grades, including the unaccepted ones, should be disclosed in the prospectus and abridged prospectus.

iii. Guidelines for Issue of Indian Depository Receipts (IDRs)

SEBI issued Guidelines for disclosures and other related requirements for companies desirous of issuing IDR in India. The issuer company must be listed in its home country and has to satisfy conditions relating to minimum issue size and minimum subscription to the issue amongst others. SEBI also prescribed the listing requirements for entities issuing IDRs, by way of a model listing agreement.

iv. Qualified Institutions' Placement (QIP)

SEBI facilitated a fast and cost-effective way of raising funds from the Indian securities market by way of private placement of securities or convertibles (but not warrants) with the Qualified Institutional Buyers. This is termed as Qualified Institutions' Placement (QIP) (Box 1.2). In case of QIP, the issuer is not required to file a draft offer document with SEBI, which saves both time and cost.

v. Corporate Bond Market – Launch of Reporting Platform

To implement the Union Budget proposal on creation of a unified platform for trading of corporate bonds, SEBI stipulated that an authorised reporting platform be established to capture all information related to trading in corporate bonds as accurately and as close to execution as possible. SEBI mandated that both BSE and NSE should set up and maintain a reporting platform for corporate bonds.

vi. Publicity Restrictions

SEBI amended DIP Guidelines to specifically prohibit an issuer company to go for any kind of publicity, prior to filing the draft offer document with SEBI, if the advertisement/publicity is not consistent with the past practices of the company. The company can, however, undertake such publicity provided, there is a prominent disclosure about their intention to come forward with an issue, in terms of the guidelines.

Box 1.2: Qualified Institutions' Placement

SEBI vide its circular dated May 08, 2006, amended the SEBI (Disclosure and Investor Protection) (DIP) Guidelines, 2000 to introduce a new method of raising funds from market by companies in the form of 'Qualified Institutions' Placement' (QIP). It is a form of private placement. It is an attempt by SEBI to encourage Indian companies to raise money domestically rather than going outside for Foreign Currency Convertible Bonds (FCCBs)/ American Depository Receipts (ADRs)/Global Depository Receipts (GDRs). Only those companies which are listed on stock exchanges having nation wide trading terminals are allowed to raise funds by selling their securities directly to Qualified Institutional Buyers (QIBs). They may be public financial institutions as defined in section 4A of Companies Act, 1956, Scheduled Commercial banks, Mutual Funds, FIIs registered with SEBI, VCFs, FVCFs, State Industrial Development Corporations, Insurance Companies, Provident Funds having minimum corpus of Rs. 25 crore and Pension Funds having minimum corpus of Rs. 25 crore.

QIP Issue Structure

The placement size of QIPs shall not exceed five times the pre-issue net worth as per the audited balance sheet of the previous financial year. Minimum of 10 per cent of specified securities shall be allotted to mutual funds. If no mutual fund is agreeing to take up the minimum portion or any part thereof, such portion may be allotted to other QIBs. No allotment shall be made, directly or indirectly, to any QIBs being a promoter or any person related to promoters. There should be at least two allottes for an issue of size upto Rs. 250 crore and at least five allottes for an issue size in excess of Rs. 250 crore. No single allotee shall be allotted more than 50 per cent of the issue size.

Pricing & Lock-in

The pricing requirements shall be broadly at par with those for Guidelines for preferential issues as specified in the SEBI (DIP) Guidelines. Minimum price is higher than the average of the weekly high and low of the closing price quoted during six months or two weeks preceding the relevant date. There shall be adjustment of price in case of corporate actions, right issue, stock splits, etc.There will be no lock-in period for the securities allotted under this route. However, there cannot be off-market transaction in such securities for a period of one year from the date of allotment.

Payment Terms

The specified securities allotted pursuant to QIP shall be made fully paid-up at the time of their allotment.

Other Requirements

The placement document shall contain all material information, including the information specified in Chapter XIII-A of SEBI (DIP) Guidelines. Being a private document, it can be provided only to select investors through serially numbered copies. The placement document will be placed on the website of the concerned stock exchange and of the issuer. A copy of the placement document will also be filed with SEBI for record purpose, within thirty days of the allotment. A security which is convertible into or exchangeable with equity shares at a later date, may be converted or exchanged into equity shares at any time after allotment of security, but not later than 60 months from the date of allotment.

Box 1.2: Qualified Institutions' Placement *(Contd.)*

The resolution approving QIP passed under section 81(1A) of the Companies Act, 1956 will remain valid for a period of twelve months from the date of passing. QIP will be managed by a SEBI registered merchant banker who will exercise due diligence and furnish a due diligence certificate to stock exchange with all relevant requirements.

An issue may arise in this context that, by allowing the QIP due emphasis is not being given to the retail investors. The idea behind QIP is to enable listed companies to raise funds from domestic market without going to foreign countries through ADRs / GDRs. That means QIPs are giving due importance to the growth of our economy domestically. The requirement of minimum 10 per cent allotment to mutual funds is intended to help the retail investors indirectly as a large number of retail investors invest via mutual fund route.

The decision of SEBI to allow listed companies to raise funds from the domestic market through QIP will encourage corporates to consider the local market more effectively. QIP has an advantage over FPO in terms of cost, time and comparatively simpler procedures. With this, QIP is poised to be a more favourable fund-raising route for Indian companies, in the coming days, in comparison to ADRs / GDRs / FCCBs.

vii. Common Platform for Electronic Filing and Dissemination of Information for Listed Companies

In order to enhance transparency and efficiency of the securities market, SEBI advised the two major stock exchanges, BSE and NSE to explore the possibility of setting up a common electronic platform which should aim at (i) providing a single window filing to listed companies irrespective of multiple listing, (ii) eliminating paper filing with the stock exchanges, (iii) covering all listed companies (including companies listed on stock exchanges other than NSE and BSE) and (iv) being a one-stop shop for sourcing corporate information of listed companies by investors.

At the instance of SEBI, on January 01, 2007, BSE and NSE, jointly launched a common portal at www.corpfiling.co.in. This portal is jointly owned, managed and maintained by the two exchanges. In the first phase since its launch, the platform has been disseminating filings made by companies listed on these exchanges. Further, it was proposed to implement electronic filing in a phased manner and to upgrade the dissemination portal into a common filing and dissemination platform by April 01, 2007. When this arrangement will be fully operational, a company would be required to file the information only once, irrespective of the exchange(s) where it is listed. The investors will be able to access such filings from a single source irrespective of the exchange on which the shares are listed.

viii. Advisory Committees for Policy Initiatives

SEBI reconstituted two committees, namely, Primary Market Advisory Committee (PMAC) and SEBI Committee on Disclosures and Accounting Standards (SCODA).

a) PMAC was reconstituted under the Chairmanship of Shri Deepak S. Parekh, Chairman, HDFC, on July 27, 2006. In its meetings, PMAC deliberated on various topics, such as, IPO grading, systemic issues in IPO process, proposed

facility of on-line application in IPOs, recent trends in issues like lock-in of pledged shares, filing of offer documents - pending completion of restructuring, role of print media companies in issues, review of corporate governance provisions, review of guidelines governing preferential issues, review of mechanism of refund through Electronic Clearing Service (ECS) in IPOs, etc.

b) SCODA was created by merging two advisory committees of SEBI, namely, SEBI Committee on Disclosures (SCOD) and SEBI Committee on Accounting Standards (SCAS), on September 12, 2006. This Committee is chaired by Shri Y. H. Malegam. The Committee deliberated upon issues like disclosure of financials pertaining to debt issued on private placement basis, interpretation of provisions of guidelines regarding financial statements, convergence of Indian Accounting Standards with International Financial Reporting Standard (IFRS), use of Extensible Business Reporting Language (XBRL) in financial reporting, etc.

II. Secondary Securities Market

i. VaR Margining in Cash Market

In cash market, VaR margin rates were calculated at the end of the trading day and then applied to open positions for the subsequent trading day. To ensure market safety, to protect the interest of investors, and to align the risk management framework across the cash market, it was decided that the risk arrays should be updated intra-day in the cash market as is being practised in derivatives market.

Accordingly, the stock exchanges were advised to update the applicable VaR margin rates, at least five times in a day. This may be carried out by taking the closing price of the previous day- at the start of trading and the prices at 11:00 a.m., 12:30 p.m., 2:00 p.m., and at the end of the trading session.

ii. Mandatory Requirement of PAN for Trading in Cash Market

In order to further strengthen Know Your Client (KYC) norms in the cash market and facilitate reliable audit trail, PAN was made mandatory for all the entities/persons having transaction in cash market with effect from October 01, 2006.

Since, certain operational issues came up for discussion and market participants made representations, the deadline for compliance of KYC norms was extended to December 31, 2006.

iii. Mandatory Requirement of PAN for Opening and Operating Demat Accounts

PAN was made mandatory for all categories of demat account holders including minors, trusts, foreign corporate bodies, banks, corporates, FIIs and NRIs, in respect of all dematerialised accounts opened by them on or after April 01, 2006. As regards demat accounts which existed prior to April 01, 2006, time for furnishing and verification of PAN card details was granted upto December 31, 2006. The accounts of those investors who could not comply with the mandatory PAN requirement stood suspended for debit, with effect from January 01, 2007.

iv. Standing Committee for Addressing Problems in Computerised Trading

The stock exchanges were advised to set up Standing Committee to investigate the problems of computerised trading system, such as, hanging / slowdown / breakdown.

To ensure compliance on the issue raised during inspection of stock exchanges conducted by SEBI and to bring uniformity in implementation / compliance, the stock exchanges were advised, as under:

a) All instances of hanging /slowdown / breakdown and any other problem in the computerised trading system, even for disruptions less than five minutes, should be reported to the Committee for its consideration.

b) The Committee, upon examination of the issue shall submit a report to the Governing Board / Council of the stock exchange.

c) The Governing Board / Council of the stock exchange shall deliberate on the aforesaid report and take suitable action / remedial measure.

d) In case of stoppage beyond five minutes the exchange should also explain and report to SEBI about the nature of incident as well as the remedial measures taken. The stock exchange shall also issue a press release in this regard for greater transparency and in the larger interest of investors.

v. Dissemination of Tariff/Charge Structure of Depository Participants (DPs)

Following the representations by investors to SEBI that the tariff/charge structure of various DPs should be made available for comparison so as to enable investors to take an informed decision with regard to availing of the services of a particular DP, SEBI advised DPs to submit the tariff/charge structure every year, latest by April 30, to their depositories. Also, DPs should inform their depositories about the changes in their tariff/charge structure, as and when the changes are made.

The depositories were further advised to disseminate the same on their websites so as to enable the investors to have a comparative analysis of the tariff/charge structure of various DPs.

vi. Clarification on Comprehensive Investor Protection Fund (IPF)/ Customer Protection Fund (CPF)

It was clarified that in the case of a stock broker, having multiple memberships, being declared defaulter, any amount remaining to his credit, after satisfying the eligible claims at the stock exchange/SEBI/other stock exchanges, shall be credited to the IPF/CPF of respective exchange.

vii. Safeguards to Address the Concerns of the Investors on Transfer of Securities in Dematerialised Mode

Various representations were received from investors regarding transfer of securities from Beneficiary Owner (BO) Accounts without proper authorisation by the concerned investor. The following safeguards were put in place to address the aforesaid concerns:

a) The depositories to give more emphasis on investor education particularly with regard to careful preservation of Delivery Instruction Slip (DIS) by the BOs. The depositories to advise the BOs not to leave "blank or signed" DIS with the DPs or any other person/entity.

b) The DPs not to accept pre-signed DIS with blank columns from the BO(s).

c) The DPs to issue only one DIS booklet containing not more than 20 slips for individual account holders and not more than 100 slips for non-individual account holders, at a time.

d) If the DIS booklet is lost / stolen / not traceable by the BO, the same must be intimated to the DP immediately by the BO in writing. On receipt of such intimation, the DP shall cancel the unused DIS of the said booklet.

e) The DPs can issue subsequent DIS booklet to a BO only after the BO has used at least 75 per cent of the slips contained in the previous DIS booklet. The DP shall also ensure that a new DIS booklet is issued only on the basis of the DIS instruction request slip (contained in the previous booklet) duly completed in all respects, unless the request for fresh booklet is due to loss, etc.

f) The DPs not to issue more than 10 loose DIS to one account holder in a financial year (April to March). The loose DIS can be issued only if the BO(s) comes in person and sign the loose DIS, in the presence of an authorised DP official.

g) The DPs to put in place appropriate checks and balances with regard to verification of signatures of the BOs, while processing the DIS.

h) The DPs to cross check with the BOs before acting upon the DIS.

i) The DPs to mandatorily verify with a BO before acting upon the DIS, in case of an account which remained inactive, i.e., where no debit transaction had taken place for a continuous period of six months, whenever all the International Securities Identification Number (ISIN) balances in that account (irrespective of the number of ISINs) are transferred at a time. However, in case of active accounts, such verification may be made mandatory, only if the BO account has five or more ISINs, and all such ISIN balances are transferred at a time. The authorised official of the DP verifying such transactions with the BO, shall record the details of the process, date, time, etc., of the verification on the instruction slip under his signature.

viii. Reconstitution of Secondary Market Advisory Committee (SMAC)

SMAC was reconstituted under the Chairmanship of Prof. P.G. Apte in the month of November 2006. In its meetings, SMAC deliberated on various topics, such as, measures to check excess dematerialisation of securities, voluntary withdrawal by issuers and / or compulsory deactivation of ISIN by depositories, reduction of minimum contract size in the derivatives market, regulation of Investment Advisers, tightening of entry norms in F&O segment, cooling off period – post IPO, etc.

ix. Initiatives for Derivatives

a) Procedure for Re-introduction of Derivatives Contracts and Modified Position Limits:

Issues pertaining to introduction, dropping and re-introduction of derivatives contracts; market wide position limits for stock based derivatives, and position limits for index derivatives were reviewed by the Secondary Market Advisory Committee (SMAC). Based on the recommendations of SMAC, procedure for re-introduction of derivative contracts and modified position limits are as under:

- The exit criterion was made more flexible as compared to entry criteria, in order to prevent frequent entry and exit of stocks in the derivatives segment. Accordingly, for a stock to

become ineligible, the criteria for market wide position limit was relaxed upto 10 per cent of the criteria applicable for the stock to become eligible for derivatives trading. If a stock fails to meet the eligibility criterion for three consecutive months, then the stock will be dropped out of the derivatives segment.

- A stock which is dropped from derivatives trading may become eligible once again. In such cases, the stock is required to fulfil the eligibility criteria for three consecutive months (instead of one month as specified earlier) to be re-introduced for derivatives trading. Derivative contracts on such stocks may be re-introduced by the exchange itself. However, introduction of futures and option contracts on a stock for the first time would continue to be subject to SEBI approval.

b) Position Limits

➢ Market-wide Position Limits for Single Stock Futures and Stock Option Contracts:

- The market wide position limit is linked to the free float market capitalisation and shall be equal to 20 per cent of the number of shares held by non-promoters in the relevant underlying security (i.e. free float holding).

- This limit would be applicable on aggregate open positions in all futures and option contracts on a particular underlying stock.

➢ Trading Member/FII/Mutual Fund Position limits in Equity Index Option Contracts:

The trading member/FII/mutual fund position limits in equity index option contracts shall be higher of Rs. 500 crore or 15 per cent of the total open interest in the market in equity index option contracts. This limit would be applicable on open positions in all option contracts on a particular underlying index.

➢ Trading Member/FII/Mutual Fund Position Limits in Equity Index Futures Contracts:

The trading member/FII/mutual fund position limits in equity index futures contracts shall be higher of Rs. 500 crore or 15 per cent of the total open interest in the market in equity index futures contracts. This limit would be applicable on open positions in all futures contracts on a particular underlying index.

c) Setting up of Derivatives Market Review Committee:

SEBI decided to set up a 'Derivatives Market Review Committee', under the Chairmanship of Prof. M. Rammohan Rao, for carrying out a comprehensive review of the developments in the derivatives market in India. This committee would also look into the future prospects and possibilities in this area.

x. Corporatisation and Demutualisation (C & D) of Stock Exchanges

SEBI approved and notified the Corporatisation and Demutualisation Schemes of 19 stock exchangess, under Section 4B (8) of the Securities Contracts (Regulation) Act, 1956.

Accordingly, SEBI notified Securities Contracts (Regulation) (Manner of Increasing and Maintaining Public Shareholding in Recognised Stock Exchanges) Regulations, 2006 on November 13, 2006 whereby the recognised stock exchanges were directed to ensure that at least 51 per cent of its equity share capital is held by the public, either by fresh issue of equity shares to the public through issue of prospectus or in the following manner:

a) offer for sale of shares, held by shareholders, having trading rights therein, by issue of prospectus;

b) placement of shares held by shareholders having trading rights to such persons or institutions as may be short-listed by the recognised stock exchange with the approval of the SEBI Board;

c) issue of equity shares on private placement basis by the recognised stock exchange to any person or group of persons not being shareholders having trading rights or their associates subject to the approval of the SEBI Board; or

d) any combination of the above.

The Regulations further provided that:

a) no person shall, directly or indirectly, acquire or hold more than five per cent in the paid up equity capital of a recognised stock exchange at any time after commencement of the Regulations;

b) no person shall, either individually or together with persons acting in concert with him, acquire and/or hold more than one per cent of the paid up equity capital of a recognised stock exchange after commencement of the regulations, unless he is a fit and proper person and has taken prior approval of SEBI for doing so.

Further, SEBI vide circular dated December 22, 2006 communicated the policy of the Government of India on foreign investments in infrastructure companies in securities markets, namely stock exchanges, depositories and clearing corporations, whereby:

a) Foreign investment up to 49 per cent will be allowed in these companies with a separate FDI cap of 26 per cent and FII cap of 23 per cent;

b) FDI will be allowed with specific prior approval of Foreign Investment Promotion Board (FIPB);

c) FIIs will be allowed only through purchases in the secondary market;

d) FIIs shall not seek and will not get representation on the Board of Directors;

e) No foreign investor, including persons acting in concert, will hold more than five per cent of the equity in these companies.

In addition, the aforesaid limits for foreign investment in respect of recognised stock exchanges shall be subject to the limit of five per cent shareholding by any person, directly or indirectly, as prescribed under the Securities Contracts (Regulation) (Manner of Increasing and Maintaining Public Shareholding in Recognised Stock Exchanges) Regulations, 2006.

III. Mutual Funds

i. Rationalisation of Initial Issue Expenses and Dividend Distribution Procedure

In order to contain frequent churning of the investors in mutual fund schemes and to clarify expense structure in SEBI (Mutual Funds) Regulations, 1996 with greater precision, SEBI decided to rationalise the initial issue expenses. Accordingly, for the purpose of meeting the expenses connected with sales and distribution of schemes, close-

ended schemes were permitted to charge initial issue expenses to the scheme. Similarly, open-ended schemes were not permitted to charge initial issues expenses but can charge only entry load.

It was further clarified that in close-ended schemes where initial issue expenses are amortised, for an investor exiting the scheme before amortisation is completed, the asset management company (AMC) shall redeem the units only after recovering the balance proportionate unamortised issue expenses.

Also, as a step towards introducing uniform practices in procedure for dividend distribution by the mutual funds, the AMCs were advised to issue a notice to the public within one calendar day of the decision by the trustees on dividend distribution.

ii. Undertaking from Trustees for New Scheme Offer Document

To address the concerns regarding launch of similar products, mutual fund trustees were required to certify that the scheme approved by them is a new product and is not a minor modification of an existing scheme/ product. However, the said certification shall not be applicable to fixed maturity plans and close-ended schemes but shall be applicable to close-ended schemes with a feature of conversion into open-ended scheme on maturity.

iii. Revised Monthly Cumulative Report (MCR) and Annual Statistical Report (ASR)

In order to capture the trends in unit capital, the formats of MCR and ASR submitted by the mutual funds were revised.

iv. Investments in ADRs/GDRs/Foreign Securities and Overseas ETFs

Pursuant to the Finance Bill 2006-07, the aggregate ceiling for mutual fund industry to invest in ADRs/GDRs issued by Indian companies, equity of overseas companies listed on recognised stock exchanges overseas and rated debt securities was raised from USD 1 billion to USD 2 billion. Subsequently, the limit was raised to USD 3 billion by RBI. The mutual funds were also permitted to invest in overseas ETFs.

Accordingly, the maximum ceiling of such investments for individual mutual funds was raised from USD 50 million to USD 100 million and subsequently the limit was raised to USD 150 million. The mutual funds were also advised to appoint a dedicated fund manager for making such investments.

v. Introduction of Capital Protection Oriented Schemes and Revision in Fees

The SEBI (Mutual Funds) Regulations, 1996 were amended so as to permit the launch of Capital Protection Oriented schemes. The proposed portfolio structure indicated in the offer document and Key Information Memorandum (KIM) must be rated by a SEBI registered credit rating agency as per Regulation 38A of mutual fund Regulation. Moreover, the rating should be reviewed on a quarterly basis. In this regard, the trustees should also continuously monitor the structure of the portfolio of the capital protection oriented scheme and should report the same in the half-yearly trustee report. It should also be ensured that the debt component of the portfolio structure has the highest investment grade rating.

The fees payable by mutual funds to SEBI was also revised. This would be applicable to those schemes whose offer documents were filed with SEBI on or after the issue of Gazette Notification dated August 03, 2006.

vi. Uniform Cut-off Timing for Applicability of Net Asset Value (NAV)

Due to various systemic changes brought out by RBI in money market, the cut-

off timings for applicability of NAV in case of purchases and redemptions of liquid schemes were revised and comprehensive Guidelines were issued.

vii. Dispatch of Statement of Accounts

SEBI directed mutual funds to dispatch the statement of accounts to the unit holders under Systematic Investment Plan (SIP) / Systematic Transfer Plan (STP) / Systematic Withdrawal Plan (SWP) once every quarter ending March, June, September and December within ten working days of the end of the respective quarter. However, the first statement of accounts under SIP/STP/SWP shall be issued within ten working days of the initial investment.

In case of specific request received from investors, mutual funds shall provide the statement of accounts to the investors within five working days from the receipt of such request without any charges. Further, soft copy of the account statement shall be mailed to the investors under SIP/STP/SWP to their e-mail address on a monthly basis, if so desired by the investors.

SEBI further advised mutual funds to provide account statements to the unit holders who have not transacted during the last six months to ensure better information flow.

viii. Launch of Gold Exchange Traded Funds

SEBI amended the SEBI (Mutual Funds) Regulations, 1996 to specify the methodology for the valuation of gold for the purpose of Gold Exchange Traded Funds (GETFs). Accordingly, the gold held by a GETF scheme shall be valued at the AM fixing price of London Bullion Market Association (LBMA) in US dollars per troy ounce for gold having a fineness of 995.0 parts per thousand, subject to prescribed adjustments. During the year two GETF schemes were launched.

ix. Real Estate Mutual Fund (REMF)

Draft Regulations for REMF were approved by SEBI. REMF Scheme means a scheme of a mutual fund which has investment objective to invest directly or indirectly in real estate property and shall be governed by the provisions and guidelines under SEBI (Mutual Funds) Regulations. The structure of the REMFs, initially, shall be close-ended. The units of REMFs should be compulsorily listed on the stock exchanges and NAV of the scheme should be declared daily. The final framework is being worked out given the special nature of real estate as an asset class and various concerns expressed on this issue (Box 1.3).

IV. Foreign Institutional Investors

The year 2006-07 saw SEBI taking a number of steps with regard to foreign institutional investors (FIIs). The steps taken were: (i) opening of the Indian securities market to new categories of FIIs, (ii) widening the scope of investment for FIIs, (iii) simplification of registration documentation and process of registration and (iv) increase in the infrastructure facilities. A summary of the steps is given below:

a) Insurance company or reinsurance company, an international or multilateral organisation or an agency thereof, a foreign government agency or a foreign central bank and investment manager or advisor were included in the eligible categories that can be registered as FIIs.

b) Reserve Bank of India (RBI) allowed a separate limit of USD 500 million for investment by FIIs in new debt instruments qualifying for upper tier II capital of banks.

c) The investment limit for FIIs in Government Securities (including

Box 1.3: Real Estate Investment Schemes for Mutual Funds in India

Real estate is an important asset class, which is generally not available to investors in India, except through direct ownership of properties. Investment in real estate provides opportunity for capital gains as well as periodic incomes. Over a longer term real estate provides returns that are comparable with returns on equities. The volatility in prices of real estate is lower than equities leading to a better risk-return trade off for the investment. Real estate investments made over long periods of time provide an inflation hedge and yield real returns. However, real estate is distinct from other assets. The real estate investments are lumpy in nature and unaffordable to many. The specific risk is high and personal diversification is very difficult. The legal issues and lack of transparency make the probability of a mistake high. The illiquid nature of the markets makes the undoing of a wrong real estate investment a tedious and painful process. Distress sales generate much lower returns than the fair value of the property.

Professional management attempts to limit the risks in real estate investment and, at the same time, brings in such advantages as legal expertise, information on prices and regular maintenance and repairs.

Real estate investment schemes provide affordability to small investors enabling their participation in the property market. They help investors to diversify their investment portfolio across various asset classes and reduce the property specific risk. The benefits include professional management and liquidity for the investment.

Real Estate Investment Trusts (REITs) have been in existence in the United States of America since 1960. In the beginning, REITs were constrained because of the limited permission to own real estate and not operate or manage it. The provisions of the tax code which made real estate investment tax shelter-oriented also hindered the growth of REITs. The Tax Reform Act of 1986 reduced the potential for real estate investment to generate tax shelter opportunities and permitted the REITs to also operate and manage most types of income producing commercial properties. REITs became a popular way of accessing the markets during the early 1990s when property values dropped between 30-50 per cent. While the sector experienced credit crunch, REITs became the source of capital to many private real estate companies and a convenient mode for investors to gain exposure to the sector. There are about 190 publicly traded REITs in the USA and registered with the SEC, with assets totaling over USD 500 billion.

In the United Kingdom, real estate investments are done through pooled managed vehicles (PMVs), which are in the form of Trusts, having a variable capital and are similar to open-ended funds. PMVs may get tax benefits based on the investor profile. REITs are a relatively new entrant in the Asia Pacific region in Singapore, Malaysia, Hong Kong, Taiwan, Korea and Thailand.

Association of Mutual Funds in India (AMFI) had set up a Committee to study the introduction of real estate schemes for mutual funds in India. The Committee submitted its report in October 2000. AMFI subsequently appointed a Sub-Committee to formulate a working plan for launching of REMFs in India, which submitted its report in August 2002. SEBI examined the proposals and took into consideration certain concerns raised by investor associations and the Institute of Chartered Accountants of India (ICAI). On account of the well developed stage of the mutual fund industry in India, SEBI decided to allow the existing mutual funds in India to float real estate investment schemes. In June 2006, the guidelines for Real Estate Mutual Funds were approved by the SEBI Board. A real estate mutual fund scheme means a mutual fund which has investment objective to invest directly or indirectly in real estate property and shall be governed by the provisions and guidelines under SEBI (Mutual Funds) Regulations, 1996. Certain residual issues relating to valuation and accounting are being addressed.

Treasury Bills) was raised from USD two billion to USD 2.6 billion.

d) FIIs were allowed to invest in security receipts.

e) Application forms for FIIs and sub-account registration were simplified.

f) The period of registration for the FIIs was reduced from five to three years.

g) The fee for registration as FIIs and sub-account was revised from USD 5,000 and USD 1,000 to USD 10,000 and USD 2,000, respectively.

h) FIIs were allowed to settle their transaction in the physical settlement mode where the issuer of such securities has not established connectivity with all depositories registered with SEBI.

V. Custodians

SEBI initiated the following policies and programmes with respect to custodians:

a) Three new custodians (including one for custodial services of gold and gold related instruments) were registered under SEBI (Custodian of Securities) Regulations, 1996.

b) Scope of custodial services was enlarged to include safekeeping of gold or gold related instruments, consequent to introduction of gold and gold related instruments in the Indian mutual fund market.

c) Enabling provisions were made for existing custodians to provide custodial services for gold or gold related instruments subject to prior permission from SEBI.

d) Registration fee in respect of custodians was revised and a fixed period of validity of three years was introduced for the certificate of registration as a custodian.

VI. Investor Assistance and Investor Education

i. Redressal of Investors' Grievances

The Office of Investor Assistance and Education (OIAE) is the single window interface through which SEBI interacts with the investors. Investors can seek assistance of OIAE in their endeavor to address the grievances that they may have against intermediaries or listed companies. OIAE also takes on board, the views and opinions of various investor interest groups recognised as Investors' Associations and encourage their participation in policy formulation process.

SEBI has a comprehensive investor grievances handling mechanism. OIAE facilitates redressal of the grievances of investors by taking up these grievances with the respective listed companies and registered intermediaries. Investors can submit their grievances against the companies and intermediaries in any of the four offices of the SEBI i.e. Head Office at Mumbai and the three Regional Offices at Delhi, Chennai & Kolkata, irrespective of the location of the intermediary/ listed company.

The grievances can be submitted on a plain paper, on a post card, via e-mail etc. apart from the standardised printed forms that are freely available at all the offices of SEBI. SEBI also has a simple and efficient internet-based response system for investors to file their grievances for matters falling in under its purview. SEBI website offers investors a facility of checking up the status of their complaints lodged.

Dedicated investor helpline numbers are also available. Dedicated personnel, manning the helpline, guide investors in filling the grievance submission forms as well as determining the appropriate authority as their first recourse. Guidance is also provided to approach the appropriate authority, if their grievance is outside the purview of SEBI.

The grievances lodged by investors are taken up with the respective listed companies and registered intermediaries. The status of the grievances is continuously monitored and regular follow up action is taken based on the response received from the companies and intermediaries.

Up to March 31, 2007, 38 companies were referred for adjudication proceedings under Section 15C of the SEBI Act, 1992 for levying penalty for failure to redress investors grievances.

On account of failure of the companies to pay the penalty imposed by the Adjudicating Officers, prosecution proceedings were initiated against 13 companies and their 70 directors, under section 24 (2) of the SEBI Act, which provides for "punishable with imprisonment for a term which shall not be less than one month but which may extend to both 10 years or with fine which may extend to Rs. 25 crores or with both".

Twelve companies and their 54 directors were debarred from accessing the capital market for a period of five years. Prosecution proceedings were initiated against 41 companies and their directors for violations pertaining to non redressal of the grievances under the provisions of the companies falling within the jurisdiction of SEBI.

During the period 1991-92 to 2006-07, SEBI received 29,07,053 grievances from investors, of which a total of 27,40,959 grievances were redressed by the respective entities, indicating a redressal rate of 94.28 per cent (Table 1.4).

ii. Enabling Investors through Awareness

As '*An Educated Investor is a Protected Investor*', SEBI continued its endeavour to enhance investor awareness. Screening of the audio-visual clippings and distribution of educative materials in English, Hindi, and local languages was carried out at the workshops, seminars, camps and lectures organised to increase awareness of the investors.

The objectives of these workshops were two fold: (a) providing enriching experience for the investors having a prior investing experience by interaction with the subject experts and (b) guiding potential investors to take first steps towards their interaction with the stock market. SEBI officers and subject experts regularly interacted with the investors in such events. SEBI partnered with the recognised investor associations for increasing the reach of these events.

SEBI has a dedicated investor website http://investor.sebi.gov.in. The investors can tap this source for all relevant information that they may require, such as, frequently asked questions on various topics, dos and don'ts for various activities in securities market, addresses of SEBI registered intermediaries, standardised complaint forms, etc.

SEBI also publishes reading and presentation materials aimed at enabling the investors to take informed decisions. In addition to the reading and presentation materials, SEBI distributed reference guides on topics, such as, rights and responsibilities of investors, mutual funds, investment in public offers, substantial acquisition of shares and takeovers, etc. These reference materials were also made available in Hindi. In addition, the workshop material was made available in 10 regional languages to enhance the reach of these messages.

iii. Recognition to Investors' Associations

The Regional Offices of SEBI were actively involved in the process of encouraging investors' association to seek recognition from SEBI. The success of this endeavour is evident as the number of

Table 1.4: Redressal of Investors' Grievances

Financial Year	Grievances Received		Grievances Redressed		Redressal Rate Percentage (cumulative)
	During the Year	Cumu-lative	During the Year	Cumu-lative	
1	2	3	4	5	6
1991-92	18,794	18,794	4,061	4,061	21.61
1992-93	1,10,317	1,29,111	22,946	27,007	20.92
1993-94	5,84,662	7,13,773	3,39,517	3,66,524	51.35
1994-95	5,16,080	12,29,853	3,51,842	7,18,366	58.41
1995-96	3,76,478	16,06,331	3,15,652	10,34,018	64.37
1996-97	2,17,394	18,23,725	4,31,865	14,65,883	80.38
1997-98	5,11,507	23,35,232	6,76,555	21,42,438	91.74
1998-99	99,132	24,34,364	1,27,227	22,69,665	93.24
1999-00	98,605	25,32,969	1,46,553	24,16,218	95.39
2000-01	96,913	26,29,882	85,583	25,01,801	95.13
2001-02	81,600	27,11,482	70,328	25,72,129	94.86
2002-03	37,434	27,48,916	38,972	26,11,101	94.99
2003-04	36,744	27,85,660	21,531	26,32,632	94.51
2004-05	54,435	28,40,095	53,361	26,85,993	94.57
2005-06	40,485	28,80,580	37,067	27,23,060	94.53
2006-07	26,473	29,07,053	17,899	27,40,959	94.28

investor associations recognised by SEBI has gone up from 10 in the last year to 18 this year.

SEBI enables these associations by providing them with resources in the form of finance, resource personnel, publications, etc. These institutions act as the extended arms of SEBI for reaching out to the investors for investor assistance and education. Resource personnel and subject experts from SEBI are made available to these Investor Associations for their workshops, seminars, camps, etc.

Investors' Associations recognised by SEBI, were, as under:

- Consumer Education and Research Society, Ahmedabad;
- Consumer Unity and Trust Society, Jaipur;
- Investor Education and Welfare Association, Mumbai;
- Investors Grievances Forum, Mumbai;
- Midas Touch Investors Association, Kanpur;
- Tamilnadu Investors Association, Chennai;
- The Gujarat Investors and Shareholders Association, Ahmedabad;
- Rajkot Sahar/Jilla Grahak Suraksha Mandal, Rajkot;
- Kolhapur Investors' Association, Kolhapur; and

- Society for Consumers' and Investors' Protection, New Delhi;

The following eight investors' associations were recognised during 2006-07:

- Karimpur Social Welfare Society, West Bengal;
- The Bombay Shareholders Association, Mumbai;
- Orissa Consumers' Association, Cuttack;
- Ganga Jamuna, Delhi;
- Mizoram Consumers' Association, Aizwal;
- Federation of Consumer Associations, West Bengal;
- Consumer Association of Pondicherry; and
- All Gujarat Investor Protection Trust, Ahmedabad.

VII. Retrospect and Prospects

i. Retrospect

So far, Indian economy has continued to sustain a high rate of growth during the Tenth Plan period. There was a robust growth of over 9.4 per cent during 2006-07. The continued momentum in manufacturing and service sector resulted in higher capacity utilisation and increased business confidence.

The investors' confidence was also reflected in the activities in the stock market. The stock market continued to gather momentum with the BSE Sensex crossing the 12,000 mark for the first time on April 29, 2006. Thereafter, it crossed 13,000 mark on October 10, 2006 and 14,000 mark on January 12, 2007, respectively. During 2006-07, BSE Sensex gained 15.9 per cent. Backed by strong macro-economic fundamentals, the overall market sentiment was buoyant throughout the year, except in June 2006 and February 2007. Reflecting the price appreciation, market capitalisation to GDP ratio and the traded value to GDP ratio increased to 85.9 per cent and 70.4 per cent, respectively in 2006-07 from 84.7 per cent and 67.0 per cent a year ago. The rally in stock market was broad based with all the sectors registering gains. Besides FIIs, mutual funds and retail investors were also active in the secondary market.

The primary market witnessed continued activity during 2006-07. The number of companies accessing the primary market was 124 compared to 139 during 2005-06. The amount mobilised was Rs. 33,508 crore during 2006-07, higher than Rs. 27,382 crore mobilised during 2005-06. The number of IPOs decreased in 2006-07. The number of rights issue in 2006-07 increased to 39 from 36 in 2005-06.

There was an increase in the mobilisation of resources by the mutual funds in 2006-07. With private sector mutual funds dominating the resource mobilisation efforts, the net resources mobilised by all mutual funds were higher at Rs. 93,985 crore during 2006-07 compared to Rs. 52,779 crore in 2005-06. The exposure of mutual funds to the debt segment increased, commensurate with higher mobilisation of resources under various debt schemes.

The FIIs continued to invest in Indian market. The number of SEBI registered FIIs went up to 997 by end March 2007 from 882 a year ago. Their net investment in equities was USD 5,474 million in 2006-07 as against USD 10,981 million a year earlier.

ii. Prospects

In an integrated market economy, regulating various market intermediaries on an individual basis to ensure investor protection and smooth functioning of the

market is a challenging task for a regulator. The job of a regulator becomes relatively easy if other organisations start to function as self-regulated entities by framing their own laws and bye-laws to keep a first level check on their registered members. In this way, while the intermediary organisations take the responsibility of a first level regulator, the central regulator acts as a second line of protection against fraud and manipulations. This not only saves time but also enables the central regulator to focus upon bigger issues of regulating and developing a vibrant securities market with all the safety nets in place.

SEBI, in an effort to develop a well regulated and orderly securities market, has been trying to promote the idea of self regulatory organisations for various market participants for sometime. In this direction, SEBI (Self Regulatory Organisations) Regulations, 2004 were notified on February 19, 2004 with the objective to promote self-regulatory organisations of intermediaries representing a particular segment of the securities market as a self regulated entity. Initiatives were taken in getting entities registered as an SRO. SEBI held meetings with the representatives of Association of NSE Members of India (ANMI) and merchant bankers and emphasised the need of having an SRO which would act as first level of regulator and provide effective checks and balances for developing a sound and integrated stock market (Box 1.4).

Box 1.4: Self Regulatory Organisations

A stable and effective financial system provides the foundation for timely implementation of policies, appropriate pricing of risk and efficient use of capital. This requires proper regulation of the financial markets as a whole. Self-regulation is a combination of private interests with regulatory oversight.

It is an effective form of regulation for the complex and dynamic financial markets. As per the IOSCO's seminal report (September 1998) on Objectives and Principles of Securities Regulation, "Self-regulatory Organisations (SROs) can be a valuable component to the regulator in achieving the objectives of securities regulation."

The scope of self-regulation varies across the developed and the emerging markets. In its absolute sense, self-regulation encompasses the authority to create, amend, implement and enforce rules of conduct with respect to the entities subject to the SRO's jurisdiction; and to resolve disputes either through arbitration or through other means.

The reason for promoting intermediaries like stock exchanges as SROs is that these entities have a better knowledge of the ground realities and, they can take better care of micro aspects of regulation. Self-regulation not only minimises the cost of regulation and compliance but it also provides the flexibility to bring about regulatory changes in a rapidly changing business environment. For an SRO to be credible and effective, it should be:

- *Independent - both in perception and in reality - from the influence of entities it regulates.*
- *Able to develop standards that are meaningful and broadly acceptable.*
- *Recognised as legitimate and relevant by the industry and by its regulators.*
- *Able to provide fair enforcement.*

In the United States, the Securities and Exchange Commission (SEC) has primary responsibility for regulating securities markets. The SEC, however, delegates significant regulatory authority to

Box 1.4: Self Regulatory Organisations *(Contd.)*

SROs, securities industry organisations that are owned and operated by their members. Examples include the National Association of Security Dealers (NASD), the New York Stock Exchange (NYSE), the Chicago Board Options Exchange (CBOE), and regional stocks and options exchanges.

In United Kingdom, SROs were set up to regulate companies dealing with investment business with the objective of investor protection as per the Financial Services Act, 1986. Some of the SROs in U.K. are Securities and Futures Authority (SFA), Investment Management Regulatory organisation (IMRO), Personal Investment Authority (PIA). Hong Kong also followed the concept of SROs as followed in U.K. Two important SROs in Hong Kong are Stock Exchange of Hong Kong (SEHK) and Hong Kong Futures Exchange (HKFE).

As the concept of self regulatory bodies is becoming increasingly popular in international jurisdictions, the structure, functions and governance methodology of these SROs like NASD, Japan Securities Dealers Association (JSDA), Korea Securities Dealers Association (KSDA) etc. is being considered by SEBI.

In India, SEBI is promoting development of self-regulatory organisations. SEBI notified SEBI (Self Regualtory Organisation) Regulations 2004 on February 19, 2004. SEBI prescribed certain eligibility criteria for registration as an SRO, which include:

- *The applicant should be a company which has been granted license under section 25 of the Companies Act, 1956.*
- *The applicant has a net worth of Rupees one crore.*
- *The applicant has, adequate infrastructure to enable it to discharge its function as an SRO.*
- *The applicant has in its memorandum of association specified admission of members and discharging the functions of an SRO as one of its main objects.*
- *The applicant and its directors have the professional competence, financial soundness, and general reputation of fairness and integrity to the satisfaction of SEBI.*
- *The applicant, in all other respects, is a fit and proper person for the grant of a certificate; and*
- *The grant of certificate to the applicant is in the interest of investors and the securities market.*

The Board of an SRO would be independent, as majority of directors are required to be independent directors. The SRO would also provide arbitration mechanism for resolving disputes among members and/or between members and their constituents; and take disciplinary action against the members for breach of governing norms. The major functions and responsibility of an SRO are as follows:

- *Ensuring investor protection, education of investors or its members, and observance of securities laws by its members.*
- *Specifying standard of conduct for its members, and responsibility of the implementation of the same by its members.*

Box 1.4: Self Regulatory Organisations *(Contd.)*

- *Making endeavours for introduction of the best business practices amongst its members.*
- *Complying with the norms of corporate governance, as applicable to the listed companies.*

SEBI is in dialogue with various associations of intermediaries for their registration as SROs. Few associations like the Association of NSE Members of India (ANMI) and Depository Participant Association of India (DPAI) have shown interest in getting themselves registered as SRO. In this regard, SEBI is considering various models of self–regulation for intermediaries.

The successful implementation of the elements of self-regulation depends on maturity and sophistication of the market; and its regulatory environment. As an SRO demonstrates its effectiveness, a successful self-regulatory programme can be implemented over time. SROs are motivated to act responsibly, develop best practices and monitor their markets. SRO functions should be developed, retained, and maximized to the extent possible, subject to appropriate accountability mechanisms to ensure proper disposal of regulatory responsibilities. When properly implemented, self regulation can lead to effective implementation of rules with wide compliance. Self-regulation is not "deregulation"; it is an important part of efficient regulation.

SEBI, with a mandate to promote and develop an orderly and secure stock market for all classes of investors strongly promoted the idea of demutualised stock exchanges in line with international best practices, where the management functions of the exchanges were separated from ownership and trading rights through demutualisation. Post-demutualisation, the central problem appears to be the fate of various regional stock exchanges (RSEs) where trading activities have become minimal. RSEs were created in the past to facilitate regional companies to raise resources for their growth objectives. It is in this regard a Committee was formed under the Chairmanship of Shri G. Anantharaman, Whole Time Member, SEBI, to come up with recommendations for productive utilisation of available infrastructure with RSEs and to provide an exit option for them (Box 1.5). Steps are being taken to implement Anantharaman Committee recommendations.

The investment community in India got a fillip as SEBI approved the draft Guidelines for real estate mutual funds (REMFs). The scheme of an REMF will be able to either invest directly or indirectly in real estate property. The REMF will be governed by the provisions and guidelines under SEBI (Mutual Funds) Regulations. The schemes will enable various classes of investors to indirectly participate in the real estate sector in India by providing an investment opportunity. The schemes will be initially close-ended where the units of REMF schemes shall be compulsorily listed on the stock exchanges and NAV of the scheme will be declared daily.

Hon'ble Finance Minister proposed several initiatives in the Budget for 2007-08 for strengthening the capital market. PAN was made as the sole identification number for all participants in the securities market with an alpha-numeric prefix or suffix to distinguish a particular kind of account. To

Box 1.5: Future of the Regional Stock Exchanges: Post De-mutualisation

The basic intention of establishing the Regional Stock Exchanges (RSEs) was to enable regional companies to raise capital and to spread the awareness about stock market investment amongst investors across the country. However, with emergence of competition among exchanges aided by globalisation and technological change, the survival of RSEs was threatened. One central problem with the RSEs was that there are very few liquid shares traded on these Exchanges. With the extension of screen-based trading network of NSE and BSE across the country, majority of the RSEs became redundant. Moreover, with a view to enhancing corporate governance, all stock exchanges have been undergoing the process of corporatisation and demutualisation.

Now, with most of the RSEs completing the process of corporatisation and demutualisation, it becomes necessary to examine their role and relevance in the changed circumstances. For productive utilization of the available infrastructure of these RSEs and making suitable recommendations about their future, a Committee was constituted under the Chairmanship of Shri G. Anantharaman, Whole Time Member, SEBI. The major recommendations of the Committee are:

- *All the RSEs whose recognition has not been withdrawn, either voluntarily or compulsorily, must collectively choose either the BSE model or the Inter-Connected Stock Exchange (ISE) model;*
- *In case both of the above models are not successful for any reasons, there would be no merit in the continuation of the RSEs. In such a case the recognition of all the RSEs will, have to be compulsorily withdrawn.*
- *Once the RSEs have chosen a particular model, those RSEs which are unwilling to accept that model will have to face compulsory withdrawal of recognition in the future as they provide neither a trading platform nor serve any public interest;*
- *In case of the subsidiaries of the RSEs whose recognition is not withdrawn, the RSEs should preferably cease to have any shareholding in the subsidiary within a period of three years. However, the RSEs may be allowed to retain less than 15 per cent of the shareholding in the spun off entity;*
- *Any entity other than exchange, multilateral agency, insurance company, bank, depository, and clearing corporation can be allowed to hold less than 15 per cent of the share capital and voting rights of the stock exchange, either singly or collectively, along with persons acting in concert. However, in case, a strategic partner is an exchange, a multilateral agency, an insurance company, a bank, a depository, or a clearing corporation, it would be allowed to hold up to a maximum of 26 per cent of the share capital and voting rights of the stock exchange either singly or collectively, along with persons acting in concert.*
- *Any strategic partner must comply with SEBI (Criteria for Fit and Proper Person) Regulations, 2004. The holding by any foreign entity, including FIIs, would be subject to the overall policy of the Government on FDI. These recommendations would have to be incorporated suitably in the divestment regulations to be framed and notified by SEBI.*
- *Self-listing should be permitted, either through the IPO route or by way of listing with appropriate exemptions from Rule 19(2)(b) of Securities Contracts (Regulation) Rules, in case, a stock exchange does not make a public offer. The regulatory conflicts, which are likely to arise, will have to be dealt with by suitable provisions in the listing agreement of the stock exchanges. The stock exchanges will have to fully comply with the provisions of corporate governance incorporated in clause 49 of the listing agreement. Overseas listing will also be permitted after the exchange has been listed on the domestic exchange.*

promote the idea of SROs for different market participants, SEBI was mandated to make regulations and if necessary, an enabling law as needed. Mutual funds were permitted to launch and operate dedicated infrastructure funds to promote the much needed flow of investment into the sector. Other major proposals were: (a) convergence of different regulations that allow individuals and Indian mutual funds to invest in overseas securities by permitting individuals to invest through Indian mutual funds; (b) allowing short selling settled by delivery, and securities lending and borrowing to facilitate delivery by institutions; and (c) putting in place an enabling mechanism to permit Indian companies to unlock a part of their holdings in group companies for meeting their financing requirements by issue of exchangeable bonds.

Keeping in view the Budget proposals and also to pursue the on-going reform initiatives as discussed above, the major items on SEBI's agenda during 2007-08 would be, as follows:

a) Providing final shape to the issue of Unique Identification Number (UIN) by making PAN as the sole identification number;

b) Promoting self regulatory organisations by way of creating new regulations and an enabling law;

c) Reviewing mutual fund regulations to pave the path for mutual funds to launch dedicated infrastructure fund for the growth of infrastructure in the country;

d) Fine-tuning the regulations to enable individuals and Indian mutual funds to invest in overseas securities;

e) Framing operational mechanisms for allowing short selling by institutional investors by delivery of securities. This has to be supplemented by Securities Lending and Borrowing Scheme to facilitate delivery;

f) Structuring regulations permitting issuance of Exchangeable Bonds by Indian companies.