**IPOs (Initial Public Offerings)**

**What is an IPO?**

An IPO is when a company which is presently not listed at any stock exchange makes either a fresh issue of shares or makes an offer for sale of its existing shares or both for the first time to the public. Through a public offering, the shares are made available to the investors at the price determined by the promoters of the company in consultation with its investment bankers.

The successful completion of an IPO leads to the listing and trading of the company's shares at the designated stock exchanges.

The past 4 years have seen an active market for IPOs. Though the number of IPOs has been small, the amounts being raised are increasing.

<table>
<thead>
<tr>
<th>YEAR</th>
<th>NO. OF IPOs</th>
<th>AMOUNT (Rs.crore)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2003-04</td>
<td>19</td>
<td>3191.10</td>
</tr>
<tr>
<td>2004-05</td>
<td>23</td>
<td>14662.32</td>
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<tr>
<td>2005-06</td>
<td>76</td>
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<tr>
<td>2006-07</td>
<td>76</td>
<td>23706.16</td>
</tr>
<tr>
<td>2007-08</td>
<td>84</td>
<td>41323.45</td>
</tr>
<tr>
<td>2008-09</td>
<td>21</td>
<td>2033.99</td>
</tr>
</tbody>
</table>

**IPOs (Initial Public Offerings)**

**Why does a company make an IPO?**

Going public provides an opportunity to the companies to raise cash for setting up a project or for diversification/expansion or sometimes for working capital or even to retire debt or for potential acquisitions. This is called fresh capital. Companies also go public to provide a route for some of the existing shareholders including venture capitalists to exit fully or partially from the company.

Given below is the table of moneys raised through issue of fresh capital and through offers for sale in IPOs.

<table>
<thead>
<tr>
<th>YEAR</th>
<th>FRESH CAPITAL</th>
<th>OFFERS FOR SALE</th>
<th>TOTAL</th>
</tr>
</thead>
<tbody>
<tr>
<td>2003-04</td>
<td>16</td>
<td>1183.42</td>
<td>5</td>
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<tr>
<td>2004-05</td>
<td>21</td>
<td>8099.59</td>
<td>9</td>
</tr>
<tr>
<td>2005-06</td>
<td>76</td>
<td>11303.21</td>
<td>11</td>
</tr>
<tr>
<td>2006-07</td>
<td>74</td>
<td>22749.44</td>
<td>12</td>
</tr>
<tr>
<td>2007-08</td>
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</tr>
<tr>
<td>2008-09</td>
<td>21</td>
<td>1985.08</td>
<td>3</td>
</tr>
</tbody>
</table>
Listing offers several benefits. For one, it increases the company's ability to raise debt at lower rates. The company also gets a continuing window for raising more capital, both from the domestic and overseas equity markets. Listing also lends liquidity to the stock, which is very critical for the success of employee stock ownership plans, which help to attract top talent. Of course, listing carries a considerable degree of prestige for the company.

Regulations for IPOs

Because of the public participation, SEBI oversees that such companies act in a reasonable and fair manner, especially with reference to the minority shareholders. For example, such companies should have a board of directors, where at least half the members are independent of the promoters/company. Moreover, companies must have a board of directors, where at least half the members are independent of the promoters/company.

SEBI’s Role in IPOs

Any company making an IPO is required to file a draft offer document with SEBI for its observations. Officials of SEBI at various levels examine the compliance with DIP guidelines and ensure that all necessary material information is disclosed in the draft offer document.

The validity period of SEBI's observation letter is three months only, i.e., the company has to open its issue within three months period.

Does it mean that SEBI recommends an issue?

SEBI does not recommend any issue nor does it take any responsibility either for the financial soundness of any scheme or the project for which the issue is proposed to be made or for the correctness of the statements made or opinions expressed in the offer document.

Does SEBI approve the contents of the offer document?

SEBI provides a clearance tag which is generally adequate and is in conformity with SEBI guidelines for disclosures and investor protection.

Does SEBI clearance tag make the IPO safe for the investors?

The investors should make an informed decision purely by themselves based on the contents disclosed in the offer document. SEBI does not associate itself with any issue/issuer and should in no way be construed as a guarantee for the funds that the investor proposes to invest through the issue. However, the investors are not absolved of the responsibility to exercise due diligence and take a decision in the light of the facts and figures disclosed in the offer document.

Eligibility norms for making an IPO

SEBI has stipulated the eligibility norms for companies planning an IPO which are as follows:

a) Net tangible assets of at least Rs. 3 crore for three full years
b) Distributable profits in at least three years
c) Net worth of at least Rs. 1 crore in three years
d) The issue size should not exceed 5 times the pre-issue net worth
e) If there has been a change in the company's name, at least 50 per cent of the revenue for preceding one year should be from the new activity.

Alternative routes

Recognizing that many good companies, for one reason or the other, may not be able to comply with all the eligibility norms, two other alternative routes are available to such companies:

Alternative I:

(a) Issue shall be through book building route, with at least 50% to be mandatory allotted to the Qualified Institutional Buyers (QIBs).
(b) The minimum post-issue face value capital shall be Rs. 10 crore.

OR

Alternative II:

(a) The "project" is appraised and participated to the extent of 15% by FIs/Scheduled Commercial Banks of which at least 10% comes from the appraiser(s).
(b) The minimum post-issue face value capital shall be Rs. 10 crore or there shall be a compulsory market-making for at least 2 years. In addition to satisfying the aforesaid eligibility norms, the company has to incorporate in the offer document.

Exemptions to certain category of entities from the eligibility norms

The following categories of entities are eligible for exemption from entry norms.

(a) Private Sector Banks
(b) Public sector banks
(c) An infrastructure company whose project has been appraised by a PFI or IDFC or IL&FS or a bank which was earlier a PFI and not less than 5% of the project.

Disclosures/Offer Documents

Since 1992, the entire IPO regulation is driven by disclosures—inform the investors as much as is possible and is relevant for him to take an informed investment decision. The disclosure requirements regarding the issuance of securities are covered in detail in the SEBI (Disclosure and Investor Protection) Guidelines, 2000.

Types of offer documents

Draft offer document refers to the first document filed by companies with SEBI and stock exchanges for approval, who after reviewing, communicate their observations to the Company, which the company has to incorporate in the offer document. SEBI typically requires a period of 30 days for processing a draft offer document.
A red herring prospectus (RHP) is a preliminary registration document that is filed with SEBI in the case of bookbuilding issue 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 are as 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.

Offer document means the final prospectus in the case of a public issue/offer for sale which is filed and registered with the Registrar of Companies and the stock exchanges. An offer document covers all the relevant information required to be disclosed under various regulations and incorporates the observations of the Re.

Abridged Prospectus means the memorandum as prescribed in Form 2A under sub-section (3) of section 56 of the Companies Act, 1956. It contains all the salient features of a prospectus. It accompanies the application form of public issues.

Accessing draft offer documents before even the IPO is cleared by SEBI
The draft offer document/letter of offer remains posted on SEBI website for a period of 21 days from the date of filing the same to SEBI and can also be downloaded from there.

Public comments/complaints on the issuer company or others connected with the issue
The objective of making an offer document public is to invite public comments. The comments should be submitted within 21 days of the filing of the draft offer document by the company with SEBI.

Obtaining full copy of the offer document
Full copy of the offer document is available from the company, its lead managers and syndicate members. These are also available on the websites of SEBI, the lead managers, the stock exchanges and the company.

Pricing
Any restrictions on price by companies?
Since 1992, companies have been allowed to freely price their issues. SEBI does not play any role in deciding the price for issues. As such, the single prices in case of fixed price issue as well as the price band in the case of a bookbuilding issue are determined by the company. The companies are however required to give in the issue price.

Differential pricing
Price of an issue where one category is offered shares at a price different from the other category is called differential pricing. In DIP Guidelines, differential pricing is allowed only if the securities to applicants in the firm allotment category are at a price higher than the price at which the net offer to the public is made. The

Types of Issues: Fixed Price & Bookbuilding
There are two types of issues:

Fixed Price issues
An issuer company is allowed to freely price the issue. The basis of issue price is disclosed in the offer document where the issuer discloses in detail about the qualitative and quantitative factors justifying the issue price. The Issuer company can mention a price band of 20% (cap in the price band should not be more than 2)

Price discovery through book building process
"Book Building” means a process undertaken by which a demand for the securities proposed to be issued by a body corporate is elicited and built up and the price for the securities is assessed on the basis of the bids obtained for the quantum of securities offered for subscription by the issuer. This method provides an op

The process is named so because it refers to collection of bids from investors, which is based on a price range. The issue price is fixed after the closing date of the bid.

A company planning an IPO appoints a merchant bank as a book runner. A particular time frame is fixed as the bidding period. The book runner then builds an order book that collates bids from various investors. Potential investors are allowed to revise their bids at any time during the bidding period. At the end of bidding

Bookbuilding has become the preferred route of raising capital, as can be seen from the table below. Though there are fixed price issues, by amount, the bookbuilding IPOs dominate.

<table>
<thead>
<tr>
<th>YEAR</th>
<th>BOOKBUILDING</th>
<th>FIXED PRICE</th>
<th>TOTAL</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>NO. OF IPOs</td>
<td>AMOUNT (Rs.crore)</td>
<td>NO. OF IPOs</td>
</tr>
<tr>
<td>2003-04</td>
<td>9</td>
<td>2641.04</td>
<td>82.8</td>
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</tr>
<tr>
<td>2007-08</td>
<td>74</td>
<td>41968.88</td>
<td>99.4</td>
</tr>
<tr>
<td>2008-09</td>
<td>17</td>
<td>1959.92</td>
<td>98.4</td>
</tr>
</tbody>
</table>

Open bookbuilding
In book-built issues, it is mandatory to have an online display of the demand and bids during the bidding period. This is known as open book system. (Under closed book building, the book is not made public and the bidders have to take a call on the price at which they intend to make a bid without having any information -

Price band
The offer document may have a floor price for the securities or a price band within which the investors can bid. The spread between the floor and the cap of the price band cannot be more than 20%. In other words, it means that the cap should not be more than 120% of the floor price. The company decides the price band.

Floor price
Floor price is the minimum price at which bids can be made.

Cut-off price
In Book building issue, the issuer is required to indicate either the price band or a floor price in the red herring prospectus. The actual discovered issue price can be any price in the price band or any price above the floor price. This issue price is called "Cut off price". This is decided by the issuer and LM after considering the...

Final issue price
The demand at various price levels within the price band is made available on the websites of the designated stock exchanges during the entire tenure of the issue and once the issue closes, the final price is determined by the issuer and made known to the investors.

Minimum number of days for which an IPO subscription list has to remain open
In the case of fixed price issues, subscription list for public issues has to remain open for at least 3 working days and not more than 10 working days.

In case of bookbuilding issues, the minimum and maximum period for which bidding has to remain open is 3–7 working days extendable by 3 days in case of a revision in the price band.

The public issue made by an infrastructure company, satisfying the requirements in Clause 2.4.1 (ii) of Chapter II may be kept open for a maximum period of 21 working days.

Allocations in an IPO

Fixed price IPOs
There are two buckets in the fixed price IPOs: Investors applying for Rs. 1,00,000 or more and Investors applying for up to Rs. 1,00,000.

Bookbuilding IPOs
In a book built issue, allocation to Retail Individual Investors (RIIs), Non Institutional Investors (NIIs) and Qualified Institutional Buyers (QIBs) is in the ratio of 35:15:50 respectively. In case the book built issues are made pursuant to the requirement of mandatory allocation of 60% to QIBs in terms of Rule 19(2)(b) of SCRR, the...

Definition of Retail Individual Investors (RIIs)
"Retail individual investor" means an investor who applies or bids for securities of or for a value of not more than Rs. 1,00,000.

Definition of Non Institutional Investors (NIIs)
All applicants, other than QIBs or individuals applying for less than Rs. 1,00,000 are considered as NIIs. Typically, this category includes High Net worth Individuals (HNIs) and corporate bodies.

Definition of Qualified Institutional Buyers (QIBs)
QIBs are those institutional investors who are perceived to possess expertise and the financial strength to evaluate and invest in the capital markets. A QIB is defined by SEBI as:

- public financial institution as defined in section 4A of the Companies Act, 1956;
- scheduled commercial banks;
- mutual funds;
- foreign institutional investor registered with SEBI;
- multilateral and bilateral development financial institutions;
- foreign Venture capital investors registered with SEBI;
- state Industrial Development Corporations;
- insurance Companies registered with the Insurance Regulatory and Development Authority (IRDA);
- provident Funds with minimum corpus of Rs. 25 crores
- pension Funds with minimum corpus of Rs. 25 crores

These entities are not required to be registered with SEBI as QIBs. Any entities falling under the categories specified above are considered as QIBs for the purpose of participating in primary issuance process.

Understanding an offer document
This section basically deals with the contents in an offer document, to enable an investor navigate through it.

Cover Page
The Cover Page of the offer document covers full contact details of the issuer company, lead managers and registrars, the nature, number, price and amount of instruments offered and issue size, and the particulars regarding listing. Other details such as Credit Rating, risks in relation to the first issue, etc are disclosed if a...
Introduction
The introduction covers a summary of the industry and business of the issuer company, the offering details in brief, summary of consolidated financial, operating and other data.

General information about the company, the merchant bankers and their responsibilities, the details of brokers/syndicate members to the issue, credit rating (in case of debt issue), debenture trustees (in case of debt issue), monitoring agency, book building process in brief and details of underwriting Agreements are given for the balance fund requirement, interim use of funds, basic terms of issue, basis for issue price, tax benefits are covered.

About us
This presents a review of the details of the business of the company, business strategy, competitive strengths, insurance, industry-regulation (if applicable), history and corporate structure, main objects, subsidiary details, management and board of directors, compensation, corporate governance, related party transactions

Financial statements
Financial statement, changes in accounting policies in the last three years and differences between the accounting policies and the Indian Accounting Policies (if the Company has presented its Financial Statements also as per Either US GAAP/IAS are presented.

Legal and other information
Outstanding litigations and material developments, litigations involving the company and its subsidiaries, promoters and group companies are disclosed. Also material developments since the last balance sheet date, government approvals/licensing arrangements, investment approvals (FIPB/RBI etc.), all government and taxation, etc.

Other regulatory and statutory disclosures
Under this head, the following information is covered: authority for the Issue, prohibition by SEBI, eligibility of the company to enter the capital market, disclaimer clause, disclaimer in respect of jurisdiction, distribution of information to investors, disclaimer clause of the stock exchanges, listing, impersonation, minimum subscription, fees payable to the registrars, underwriting commission, brokerage and selling commission, previous rights and public issues, previous issues for cash, issues otherwise than for cash, outstanding debentures or bonds, outstanding preference shares, commission and brokerage on, previous issues, capitalization act issues and mechanism for redressal of investor grievances.

Offering information
Under this head, the following information is covered: Terms of the Issue, ranking of equity shares, mode of payment of dividend, face value and issue price, rights of the equity shareholder, market lot, nomination facility to investor, issue procedure, book building procedure if applicable, bid form, who can bid, maximum subscription, book and revision of bids, price discovery and allocation, signing of underwriting agreement and filing of prospectus with SEBI/ROC, announcement of statutory advertisement, issuance of confirmation of allocation note("can") and allotment in the issue, designated date, general instructions, instructions for completing the proportionate allotment, dispatch of refund orders, communications, undertaking by the company, utilization of issue proceeds, restrictions on foreign ownership of Indian securities, etc.

Other Information
This covers description of equity shares and terms of the Articles of Association, material contracts and documents for inspection, declaration, definitions and abbreviations, etc.

Past track record of defaults/economic offences
Investors should also visit www.watchoutinvestors.com, a website aided and sponsored by the Ministry of Company Affairs under its Investor Education & Protection Fund. This website is a national registry of all entities and individuals who have been indicted by various regulators (like MCA, RBI, SEBI, BSE, NSE etc) for an economic offence.

Applying in an IPO

Prerequisites

1. Demat account
An investor has the option to apply for and receive the shares in physical form. However, it is advisable to get the allotment in demat form as the shares issued through an IPO are tradable only in the demat form. In any case, for all IPOs of any security of issue size of Rs 10 crore or more, issues have to be compulsorily dematized.

There are two depositories in the country-National Securities Depository Ltd. (NSDL) and Central Depository Services (India) Ltd. (CDSL). Both have an extensive network of authorized Depository Participants (DPs). An investor can open a demat account with any of these DPs.

The investor should fill in his the correct DP ID and Client ID details in the application forms.

2. Permanent Account Number (PAN)
Where the bids are for Rs. 50,000 or more, the bidder, or in case of a bid in joint names, each of the bidders, should mention his/her PAN allotted under the Income Tax Act. The copy of PAN card or PAN allotment letter is required to be submitted with the application form. Applications without this information and documents will not be considered.

3. Bank account/DD
Applications for IPOs are valid only if payment is made through a cheque or a demand draft. Application money cannot be paid in cash.

Process of applying in an IPO
An investor needs to first obtain an IPO application form. Forms are normally available from share brokers, lead managers, syndicate members and collecting banks. Application forms can also be picked up from the vendors at major commercial streets in most towns (for example outside the Bombay Stock Exchange).

In the case of fixed price issues, the application form along with a cheque/demand draft for the requisite amount has to be deposited with the designated collecting bankers to the issue, whose names and addresses are printed on the application form.

In the case of bookbuilding issues, the application form along with a cheque for the requisite amount has to be deposited with the designated syndicate members of the issue, whose names and addresses are printed on the application form.
Application forms should be filled carefully as incomplete/incorrect forms can be rejected due to incomplete details.

Applying for IPOs on the internet
Websites of various brokerage firms now allow the facility to their clients to apply for IPOs online.

Withdrawal of an application after the closure of an IPO
The Indian laws allow for a withdrawal of an application before the date of allotment.

Proof a bidder can request from a trading member for entering bids
The syndicate member returns the counterfoil with the signature, date and stamp of the syndicate member. The investor can retain this as a sufficient proof that the bids have been taken into account.

Changing/revising the bids
The investor can change or revise the quantity or price in the bid using the form for changing/revising the bid that is available along with the application form. However, the entire process of changing of revising the bids should be completed within the date of closure of the issue.

Knowing about IPOs currently open or are about to hit the market
Every week SEBI issues press releases for information of the public, details of offer documents filed with SEBI and observations issued.

At what price should a retail investor apply?
A retail investor is not required to make his bid at a specific price. Since he is not able to take a call on the right price, he should use the cut-off option. This would ensure that his application will be considered valid at all prices, including the final price decided by the issuer. For making bids at cut-off price, the payment has to be made at the time of placing the bid.

How to improve the chances of allotment in an IPO?
As most IPOs get oversubscribed, a retail investor is often disappointed in not getting any allotments or getting miniscule allotments. If an investor has decided on investing in a specific IPO based upon merits, he should commit as much resources as he can to that IPO. He should apply for as many shares as possible, with a realistic expectation of getting one or two allotments.

Allotments in IPOs

Firm allotments
A company making an issue to public can reserve some shares on “allotment on firm basis” for some categories as specified in DIP guidelines. Allotment on firm basis indicates that allotment to the investor is on firm basis. DIP guidelines provide for maximum % of shares which can be reserved on firm basis. The shares to be allotted in a firm allotment category is higher than the price at which securities are offered to public.

Reservations on a competitive basis
Reservation on Competitive Basis is when allotment of shares is made in proportion to the shares applied for by the concerned reserved categories. Reservation on competitive basis can be made in a public issue to the Employees of the company, Shareholders of the promoting companies in the case of a new company and development Institutions and Scheduled Banks.

Any preference while doing the allotment?
No, there cannot be any discretion in the allotment process. Prior to the SEBI Circular on DIP Guidelines dated September 19, 2005, the allotment to the Qualified Institutional Buyers (QIBs) was on a discretionary basis. This however has been amended and all allottees are allotted shares on a proportionate basis within the

Number of days for an investor to receive the refund order/allotment advice
Companies are required to finalize the basis of allotment within 30 days from the closure of the issue in case of a fixed price issue and within 45 days from the closure of the issue in case of a book building issue or else they are liable to pay interest at the rate of 15 per cent per annum. The refund orders/allotment advice is sent within 7 working days of finalization of basis of allotment. Ideally, it is around 3 weeks after the closure of the book building issue.

Key Intermediaries

Bookrunning Lead Managers/Lead Managers
A Merchant banker possessing a valid SEBI registration in accordance with the SEBI (Merchant Bankers) Regulations, 1992 is eligible to act as a Book Running Lead Manager to an issue.
In the pre-issue process, the Lead Manager (LM) takes up the due diligence of company's operations/management/business plans/legal etc. Other activities of the LM include drafting and design of Offer documents, Prospectus, statutory advertisements and memorandum containing salient features of the Prospectus. Th
other intermediaries viz., Registrar(s), Printers, Advertising Agency and Bankers to the Offer is also included in the pre-issue processes. The LM also draws up the various marketing strategies for the issue.

The post issue activities including management of escrow accounts, coordinate non-institutional allocation, intimation of allocation and dispatch of refund to bidders etc. are performed by the LM. The post Offer activities for the Offer will involve essential follow-up steps, which include the finalization of trading and dealing g refund business. The merchant banker shall be responsible for ensuring that these agencies fulfill their functions and enable it to discharge this responsibility through suitable agreements with the Company.

**Syndicate members**

The Book Runner(s) may appoint those intermediaries who are registered with the Board and who are permitted to carry on activity as an 'Underwriter' as syndicate members. The syndicate members are mainly appointed to collect and entire the bid forms in a book built issue.

**Registrar**

The Registrar finalizes the list of eligible allottees after deleting the invalid applications and ensures that the corporate action for crediting of shares to the demat accounts of the applicants is done and the dispatch of refund orders to those applicable are sent. The Lead manager coordinates with the Registrar to ensure fol
pleted and securities listed.

**Bankers to the issue**

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 Lead Merchant Banker shall ensure that Bankers to the issue are appointed in all the mandatory collection centers as specified in DIP Guidelines. The LM also ensures

The issuer discloses the addresses, telephone/fax numbers and email addresses of these intermediaries. In addition to this, the issuer also discloses the details of the compliance officer appointed by the company for the purpose of the issue.

**Filing Investor Grievances**

Most of the issue complaints pertain to non-receipt of refund or allotment, or delay in receipt of refund or allotment and payment of interest thereon. These complaints shall be made to the post issue Lead Manager, who in turn will take up the matter with registrar to redress the complaints. In case the investor does not re

Investors can also lodge their complaints at www.investorhelpline.in, a website aided and sponsored by the Ministry of Company Affairs under its Investor Education & Protection Fund.

**Other Aspects**

**Lock-in**

"Lock-in" indicates a freeze on the shares. SEBI (DIP) Guidelines have stipulated lock-in requirements on shares of promoters mainly to ensure that the promoters or main persons, who are controlling the company, shall continue to hold some minimum percentage in the company after the public issue. The requirements a

**Promoter**

The promoter has been defined as a person or persons who are in overall control of the company, who are instrumental in the formulation of a plan or programme pursuant to which the shares are offered to the public and those named in the prospectus as promoters(s). It may be noted that a director / officer of the i
promoter (i.e. any spouse of that person, or any parent, brother, sister or child of the person or of the spouse). In case promoter is a company, a subsidiary or holding company of that company; any company in which the promoter holds 10% or more of the equity capital or which holds 10% or more of the equity capital of

The details are provided in the explanatory notes to Clause 6.4.2 of the SEBI (DIP) Guidelines on Notes to Capital Structure.

**Promoter's contribution and lock-in**

In case of an IPO, the promoters have to necessarily offer at least 20 per cent of the post issue capital. In case of public issues by listed companies, the promoters shall participate either to the extent of 20 per cent of the proposed issue or ensure post-issue share holding to the extent of 20 per cent of the post-issue capital

In case of any issue of capital to the public the minimum contribution of promoters shall be locked in for a period of three years, both for an IPO and public issue by listed companies. In case of an IPO, if the promoters' contribution in the proposed issue exceeds the required minimum contribution, such excess contributio

for a period of one year from the date of allotment in public issue.

**Greenshoe option**

A 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 for a period not exceeding 30 days in accordance with the provisions of Chapter VIIA of DIP Guidelines, which is granted to a company to be exercised throu

des more probability of getting shares and also that post listing price may show relatively more stability as compared to market.

The name comes from the fact that Green Shoe Company was the first to issue this type of option.

**Safety net**

Any safety net scheme or buy-back arrangements of the shares proposed in any public issue shall be finalized by an issuer company with the lead merchant banker in advance and disclosed in the prospectus. Such buy back or safety net arrangements shall be made available only to all original resident individual allottees l

**Underwriting**

There are two types of underwriting,
Hard underwriting
Hard underwriting is when an underwriter agrees to buy his commitment at its earliest stage. The underwriter guarantees a fixed amount to the issuer from the issue. Thus, in case the shares are not subscribed by investors, the issue is devolved on underwriters and they have to bring in the amount by subscribing to the shares.

Soft underwriting
Soft underwriting is when an underwriter agrees to buy the shares at later stages as soon as the pricing process is complete. He then, immediately places those shares with institutional players. The risk faced by the underwriter as such is reduced to a small window of time. Also, the soft underwriter has the option to invoke a penalty clause in case the issue makes losses.

Primary capital market
Sale of securities by the company or its promoters through an IPO or an FPO or through rights issue is referred to as primary capital market. The shares are issued by the company to the investors against applications.

In the secondary market transactions, an investor purchases shares from another investor.

Frequently Asked Questions on IPO Grading
All details regarding operational aspects of IPO grading like, grading methodology, validity of grading, scope of grading etc., as given below are based on the information obtained from the Credit Rating Agencies (CRAs) (including their FAQs) and are meant only for general informational purpose regarding the overall functioning.

Specific details regarding IPO grading may be obtained directly from the respective Credit Rating Agencies.

What is IPO Grading?
IPO grading is the grade assigned by a Credit Rating Agency registered with SEBI, to the 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. The grade represents a relative assessment of the fundamentals of that issue in relation to other listings.

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 has been introduced as an endeavor to make additional information available for the investors in order to facilitate their assessment of equity issues offered through an IPO.

I am an issuer. By when am I required to obtain the grade for the IPO?
IPO grading can be done either before filing the draft offer documents with SEBI or thereafter. However, the Prospectus/Red Herring Prospectus, as the case may be, must contain the grade/s given to the IPO by all CRAs approached by the company for grading such IPO. Further information regarding the grading process may be obtained directly from the respective Credit Rating Agencies.

Who bears the cost of the IPO grading process?
The company desirous of making the IPO is required to bear the expenses incurred for grading such IPO.

Is grading optional?
No, IPO grading is not optional. A company which has filed the draft offer document for its IPO with SEBI, on or after 1st May, 2007, is required to obtain a grade for the IPO from at least one CRA.

Can the issuer company reject an IPO grade?
IPO grades cannot be rejected. Irrespective of whether the issuer finds the grade given by the rating agency acceptable or not, the grade has to be disclosed as required under the DIP Guidelines. However, the issuer has the option of opting for another grading by a different agency. In such an event all grades obtained for the same IPO will be displayed.

Will IPO grading delay the process of issue?
IPO grading is intended to run parallel to the filing of offer document with SEBI and the consequent issuance of observations. Since issuance of observation by SEBI and the grading process, function independently, IPO grading is not expected to delay the issue process.

What are the factors that are evaluated to assess the fundamentals of the issue while arriving at the IPO grade?
The IPO grading process is expected to take into account the prospects of the industry in which the company operates, the competitive strengths of the company that would allow it to address the risks inherent in the business (es) and capitalize on the opportunities available, as well as the company’s financial position.

While the actual factors considered for grading may not be identical or limited to the following, the areas listed below are generally looked into by the rating agencies, while arriving at an IPO grade:
- Business Prospects and Competitive Position
  - Industry Prospects
  - Company Prospects
- Financial Position
- Management Quality
- Corporate Governance Practices
- Compliance and Litigation History
- New Projects—Risks and Prospects

It may be noted that the above is only indicative of some of the factors considered in the IPO grading process and may vary on a case-to-case basis.
Does IPO grading consider the price at which the shares are offered in the issue?
No. IPO grading is done without taking into account the price at which the security is offered in the IPO. Since IPO grading does not consider the issue price, the investor needs to make an independent judgment regarding the price at which to bid for/subscribe to the shares offered through the IPO.

Where can I find the grades obtained for the IPO and details of the grading process?
All grades obtained for the IPO along with a description of the grades can be found in the Prospectus. Abridged Prospectus, issue advertisement or any other place where the issuer company is making advertisement for its issue. Further the Grading letter of the Credit Rating Agency which contains the detailed rationale for the grade obtained by the issuer can be found in the IPO Document. The Grading letter should be treated as a separate document and the same is not part of the IPO document.

Does an IPO grade, which indicates 'above average or strong fundamentals' mean I could subscribe safely to the issue?
An IPO grade is NOT a suggestion or recommendation as to whether one should subscribe to the IPO or not. IPO grade needs to be read together with the disclosures made in the prospectus including the risk factors as well as the price at which the shares are offered in the issue.

How do I interpret the IPO Grades?
The grades are allocated on a 5-point scale, the lowest being Grade 1 and highest Grade 5. The meaning of these grades have been explained under Question 1 in this FAQ.

How does IPO Grading help in deciding about investing in an IPO?
IPO Grading is intended to provide the investor with an informed and objective opinion expressed by a professional rating agency after analyzing factors like business and financial prospects, management quality and corporate governance practices etc. However, irrespective of the grade obtained by the issuer, the investor should make an independent judgment regarding the price at which to subscribe.

What is the role of SEBI in IPO grading exercise?
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.

Will IPO Grading given by CRAs be a parameter for SEBI to issue its observations?
The grading is intended to be an independent and unbiased opinion of a rating agency. SEBI does not pass any judgment on the quality of the issue company. SEBI's observations on the IPO document are entirely independent of the IPO grading process or the grades received by the company.

Which credit rating agencies are registered with SEBI?
The following four credit rating agencies are registered with SEBI.
- **Credit Analysis & Research Ltd.**
  4th Floor, Godrej Coliseum
  Somaiya Hospital Road
  Sion (East)
  Mumbai-400022
  http://www.careratings.com

- **ICRA Ltd.**
  1105, Kailash Building, 11th Floor
  26, Kasturba Gandhi Marg
  New Delhi-110 001
  http://www.icra.in

- **CRISIL Ltd.**
  CRISIL House
  121-122 Andheri Kurla Road
  Andheri (East)
  Mumbai-400093
  http://www.crisil.com

- **Fitch Ratings India Pvt. Ltd.**
  Apeejay House, 6th Floor
  3, Dinshaw Vachha Road
  Churchgate
  Mumbai-400020
  http://www.fitchindia.com

- **Brickwork Ratings India Pvt. Ltd.**
  #39/2 Sugar Complex, 2nd Floor
  Bavdhanghatta Road
  Near Diary Circle
Factors To Consider Before Investing In IPO's.

IPO's or Initial Public Offering is best understood as the first public offering of shares by a private limited company before listing in a stock market. Looking down IPO's history of success and failure stories, you would be smart to first fully understand the various aspects behind such offerings and makes the right choice to invest or not in IPO's. It is advisable to understand that investing in IPO's could prove risky with unfavorable market situations and sentiments and when the fundamentals of the company and industry are weak. It is best to go by facts, avoid being influenced by rumors and have a closer look at the past performances also.

http://www.holisticinvestment.in/before-investing-in-ipo
Regards
Ramalingam K, MBA, CFP,
Director and Chief Financial Planner,
Holistic Investment Planners
"Best Performing Financial Advisor Award" Winners from CNBC TV18
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