Legal Compliance for Incorporating Startup
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Lecture – 20
Issue of the Instruments

I welcome you in the last lecture of this particular course that is the twentieth lecture regarding Legal Compliance for Incorporating Startup, and I am in the module called Financing and Legal Compliance and I specifically talk with you regarding the Issues of Instruments. Until now, I have talked with you that how you can capitalize your business? Which form of the business can access what kind of sources of financing or funding?

Then I have talked with you that how the venture capital or private equity finance have startup. Then I said, if you wanted to go address the growth or if you have already created a good balance, you are in a good growth curve then how you can raise your fund from the financial institution. Previous then; these particular lecture I talked about that what are the instrument you can use, if you are going for issuing of this particular instrument in private placement and in primary market.

Now, which I have talked with you before that if you wanted to access the primary market or if you are accessing the private replacement, you are subjected to different regulation and the moment you are accessing the primary market, its stringent regulation is very stringent. So, I am going to talk with you now, what are the things you need to keep in mind or what are the issues you should address before you are going to issue the securities in the primary market?

Now, I believe you, by now understood what is the meaning of the securities or the instrument securities means either you are issuing the equity or the debenture or the deposit whatever it is, and the different kinds of them are basically called as the securities.

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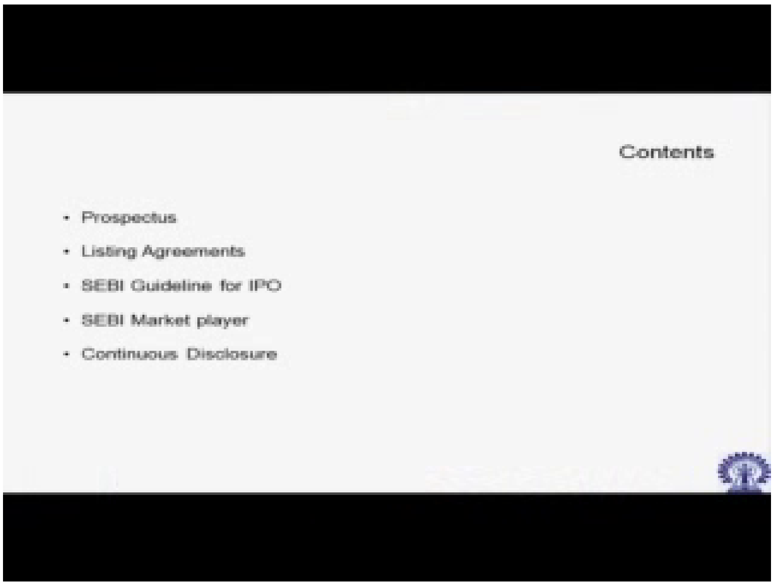

Now, in this particular lecture I am going to talk with you relating to the prospectus, then listing agreement, then SEBI guideline for initial public offer or follow public offer, and then I will talk with you SEBI market players which are known as a intermediaries and then continues disclosure.

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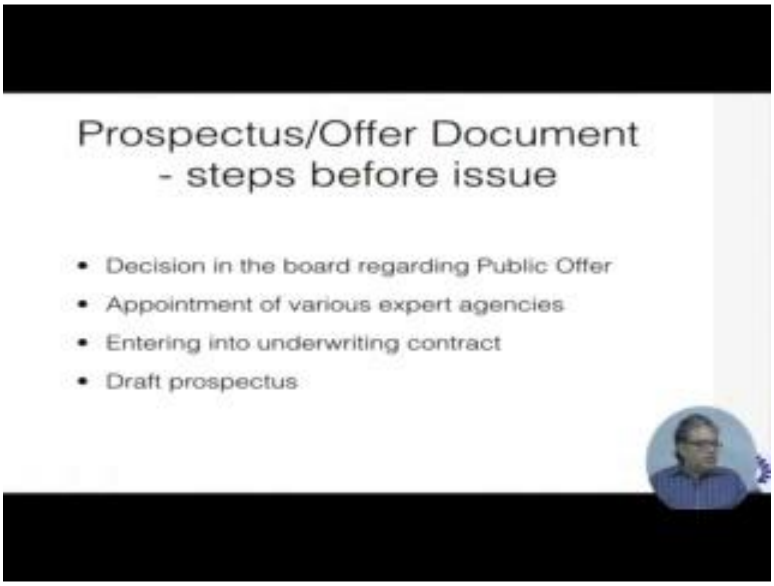

Now, let me first start with the prospectus or offer document and prospectus, and offer document is basically those document which is required to prepare before you access this market. That means it basically gives disclosure about the company, about the management, about the project which you want to initiate or for which you want to raise the fund and the risk factor which is there in your business, and which you might face while you start the initiate this particular project so much so forth. So, before you are going to offer this particular prospectus or offer document you need to take the decision in the board for the public offer that means, the board of director has to take that particular decision.

Now, again please recall my talks, I have said that whenever we are talking about the primary market we only talk about the public listed company because public listed company and public unlisted company can access the primary market, other organization cannot access this particular market; primary market. So, when I am going to refer the board, I am going to refer the board of directors of this particular public limited company either listed or unlisted.

Then you need to appoint a various expert agencies, these are generally the SEBI intermediaries which I am going to discuss with you in detail. Then you need to enter into underwriting contract. Underwriting contract means that somebody who is going to write the remaining part of the issue that means, if you are making the issue of 100 percent, let us take an example of 100 crores of rupees, then according to the SEBI regulation, 90 crores should be subscribed by the people. If 90 crores have not been subscribed then in that case the issue will fail. So, if your people has subscribed substance an amount there is a couple of percentage, like maybe 5 percent is not been subscribed by the people then in that case underwriter is subscribed those particular part and for this particular thing, generally the premium has been paid by the issuing company. So, underwriting contract is very, very important and then you need to prepare a draft prospectus.

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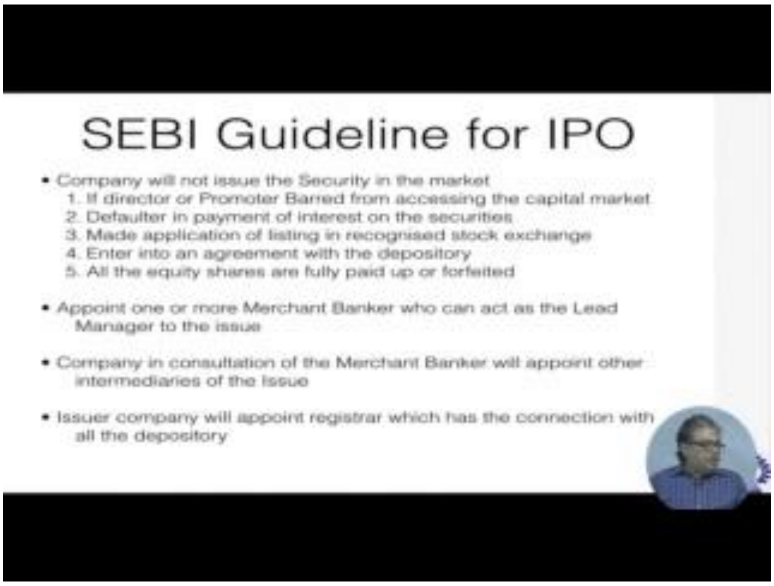

Now, in case of what I have did in this particular slide, I have tried to provide the SEBI guidelines for the IPO's and you will find there is point long listed points, which I have included within the slide. The company will not issue the security in the market if there is a certain condition which is prevalent and I have listed here, the 5.

If the directors or promoters are barred from accessing the capital market and there are several times, we will find this type of barred happened because the director is not able to pay back the interest of the debenture, which they have raised before or they have failed to pay the dividend, when the dividend has been declared or they have not complied with some of the regulations, which been prescribed either by SEBI or by some other regulator, and there is a stigma which is attached with this particular director and all this particular matter has been recorded against the director identification number in that particular circumstances, if the directors there in your board, the company cannot go for issuing of the shares. The same thing for the promoters also, what is the reputation of this particular promoter in the market?

Now, as I told you if they are defaulter in payment of the interest of the securities or the dividend, then made an application in listers, until or unless the listers agree to list your securities and then you need to enter into agreement with the depositories I am going to discuss with you, who is a depositories little later and then if all the equity shares are fully paid up or forfeited that means, whatever the equity shares which you have issued until now they have fully paid up and if it is not fully paid up or if the people have not responded to the call then those particular shares need to be forfeited.

Now, the next one is you need to appoint a merchant banker. It can be one merchant banker or two merchant bankers depending on the size of the issue it is. The very large size of the issue then in that case you need to have multiple merchant banker, then merchant banker gain consultation with the other intermediaries. The company will appoint the other intermediaries and now I am going to talk about the merchant banker and other intermediaries little later in my discussion, and then you need to appoint the registrar who is in connection with this particular depository or who is basically known as register to issue, who is examine this particular application.

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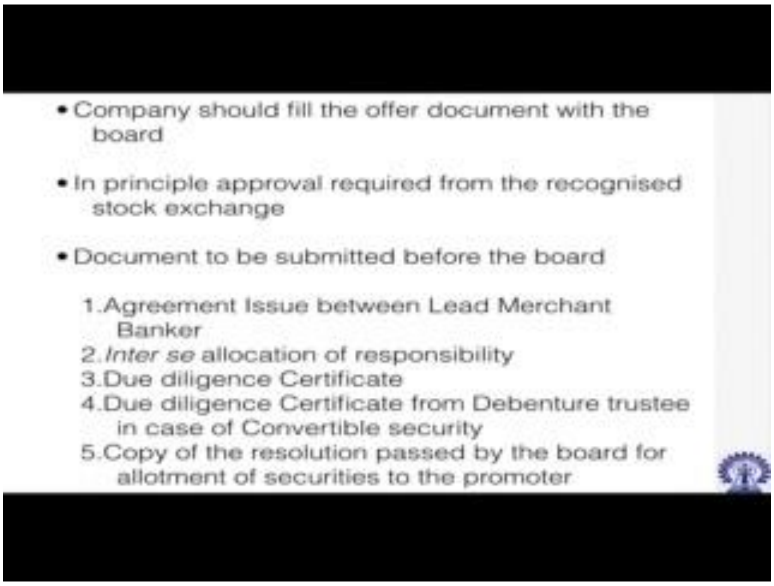

Now, company should file the offer document with the board. Board here is SEBI and SEBI is going to scrutinize this particular document, but SEBI put a disclaimer in this particular document prospectus that SEBI is no way responsible for the information, which has been stated into this particular document. SEBI is basically held merchant banker responsible if they found that whatever the rules has been specified is not been complained with. Now, the document submitted before the SEBI or the board is an agreement between the lead manager and the banker merchant. Banker then enters allocation of the responsibility that means what type of responsibility who will hold?

Then they need do the due diligence certificate means financial health relating to the company. The balance sheet of the company, then matter which I have talked with you relating to the directors credential and all those particular issue, then due diligence certificate from debenture trustee in case of a convertible debenture because you need to be a debenture.

Trustee is a person who basically takes care of the interest of all the debenture holder rather he make it sure that company do have that much of asset against which they are raising this particular loan, otherwise they will not allow to raise this particular loan as a debenture. So, debenture trustee basically ensures the interest of all debenture holders. Now, the copy of the resolution part passed by the board relating to allotment of the security to the promoters or the decision has been taken relating to rising of the capital.

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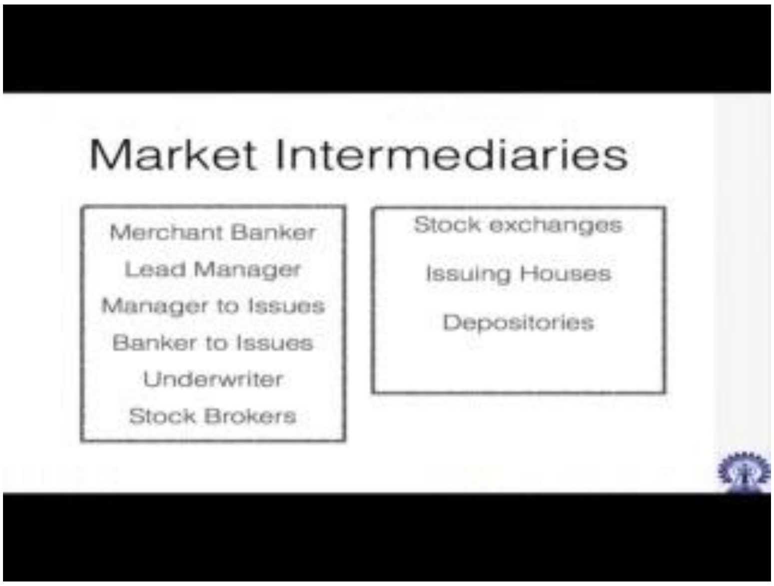

Now, let me talk with you quickly relating to the different market intermediaries. Those people who are participating in the issue are the merchant banker, lead manager, manager to issue, banker to issue, underwriter and the stock brokers. Now, merchant banker is an expert body or it is again a company or expert company who are register with SEBI and whose work is to whom to do the complaints of all the regulation, which SEBI prescribes and they are actually the people who arrange the entire issue that means, they also arrange the drafting of the prospectus.

Drafting of prospectus is a tedious document because once your organization has been grown from startup, you have a different department, different unit and different business transaction and you might have a history of this particular transaction and you need to collate all the information, when in this particular offer document. Further more you need to also analyze the different kinds of the risk, which you might face or which this particular new project is faced. So, this is a complex process and you need to have expertization for doing this particular thing and merchant banker do have this particular expertise. Now, merchant banker also appoints the other intermediaries and they also facilitating in the book running.

Book running means nowadays security is not been issued in a fixed amount that means, if you decided the face value of the security will be 10 rupees, you might charge a premium on the security. So, face value means which you actually wanted to get out of that particular issuing of the instrument, it can be 10 rupees you wanted to get, but you want to charge a premium because by now you have a reputation, you have a good business and you have a good results. So, you want some kind of a premium, whoever is making the investment because tomorrow, when these particular shares will be listed in a stock exchange, they will be traded in a high volume.

So, if people are capitalizing on these particular shares, the company who is also issuing this particular share they also wanted to get a part of particular capitalization. So, that is called a pay premium. So, you have book running; through this particular book running you decide what should be the premium for the issue and how much should be the exact price of this particular securities, then you need to talk with the lead manager.

Now, lead manager is basically again facilitate in appointment of management of this particular issue and they can also be in charge of the book running. Then manager to the issues are basically scrutinize the issues or the application banker to issues are generally take the deposit of application fees.

Application fees means wherein you have to give the amount of the shares which you wanted to purchase from that particular company through the public issue like, if the market value or the issuing price of the shares is decided in 200 rupees and if you are interested to buy around 1000 shares, then it should be 200 into 1000 rupees, you have to deposit in a bank as an application fees. So, banker to issues basically handle that particular issue, the underwriter I have talked with you, the person who basically underwrite the risk and the stock booker are those people who basically participate into trading of the shares in the secondary market.

Now, apart from that you will find that there are other people with whom you have to create the relation that is the stock exchange, where the moment, issue is complete your shares will be listed and it will be traded into the stock exchange. Now, then there is a issuing house are there. If it is small issue then in that case you issue the entire allotment to the issuing house and issuing house basically performs all the intermediary job and now, SEBI has mandated that if you are a public listed company then in that case you cannot issue the securities in a physical form. It has to be in a D-Mat form or demutualize form. So, it should be an electronic form and this particular electronic record is generally held by this electronic record held by the depositories.

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Now, I have talked with you relating to the listing agreement in the beginning of my lecture and before you go for issuing of the shares, you need to enter into a listing agreement with the stock exchange and this is actually mandated under the securities contract regulation act and they also it mandates that securities contract regulation mandate that there should be you need to, I mean enter into a listing agreement with the 2 stock exchange; one is the national stock exchange another is a regional stock exchange.

Now, national stock exchanges are the BSE, NSE and regional stock exchanges are like Kolkata stock exchange or Delhi stock exchange, Ahmadabad stock exchange. So, in 2 stock exchange you need to enter with the listing agreement because if you are not entering into the listing agreement, then you cannot go for the issuing of the shares and in with stock exchange you have entered with the listing agreement that need to be specify into the prospectors or the offer document.

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Now, listing of the agreement is important from the prospective of the corporate governance because you will find that there is a lot emphasis relating to the good compliance, lot of emphasis has been provided to relating to transparency and the accountability and listing agreement clause 49 talks about all those particular issue even though there is majority of this particular information or compliance requirement has been added under the companies act 2013, but still you will find listing agreement played a very important role because all the companies which are the public listed company, they need to submit the corporate governance report along with the annual report as part of their annual compliance and that is provided in the listing agreement.

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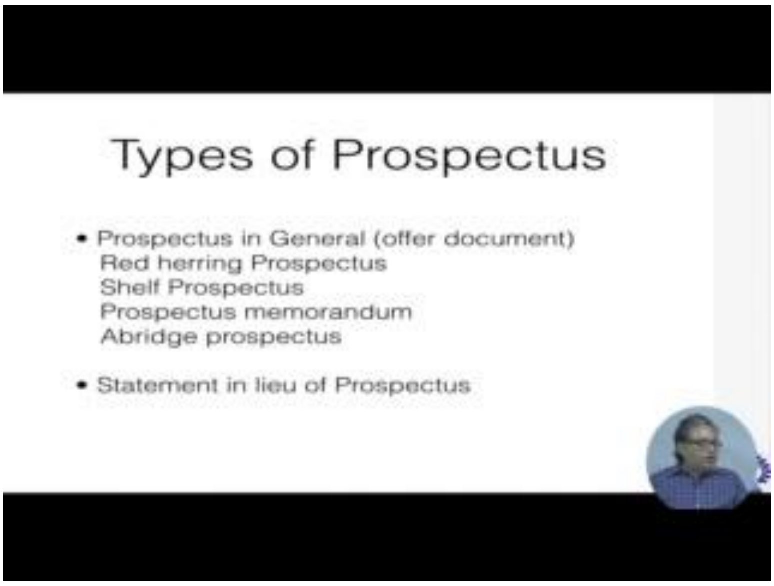

Now, let me talk with you relating to the types of prospectus. There are generally, the name of this particular prospectus I have listed here and prospectus are in generally are called offer document, also one of the SEBI regulation and then there is a red herring prospectus means the prospectus, which is incorporate incomplete with the information and this incomplete information is the issue of the price, issuing price as well as the issuing date. So, these two information missing in case of a red herring prospectus and otherwise, it is a complete prospectus then you will find there is a shelf prospectus.

Now, these particular shelf prospectuses are basically issued by the public financial institutions. They make several issues in a year, so that they can find a particular organization or particular startup or specific venture. So, if they are going to market for several times then in that case there is not much change in the prospectus which has been prepared. So, that is the reason it called a shelf prospectus that means, whenever you require you can reuse that particular prospectus by updating the information relating to the changes.

Now, there is a prospectus memorandum or abridge prospectus. These are basically the small information which you have required to provide to the; with the application form, and you might say that well, you require you can go and access the entire prospectus into a designated website, whatever it has been provided. Now, if you are going for a private placement you might, you are required to prepare the prospectus and in that case it can be a simply statement in your prospectus which is little lesser stringent in that of the offer document and prospective which I have discussed with you.

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Now, these are the step which I have noted here relating to issuing of the shares and you will find this issues of commencement of the business certificate is now taken away from the companies act, but the board has to talk about the initial public offer and then other intermediaries and all this things which I have talked with you.

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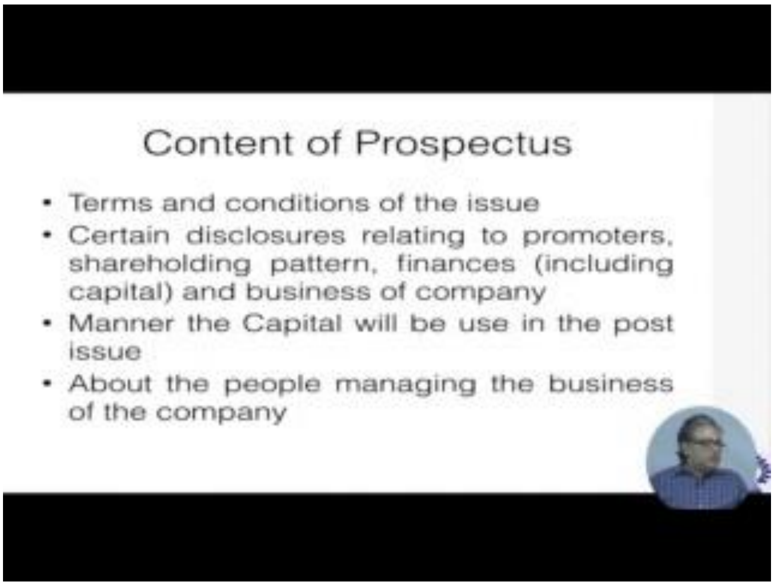

Now, in case of the content of the prospectus, you will find that you need to have a disclosure relating to the promoter, shareholding pattern, financing and the business of this company and the manner of the capital will be use in a post issue.

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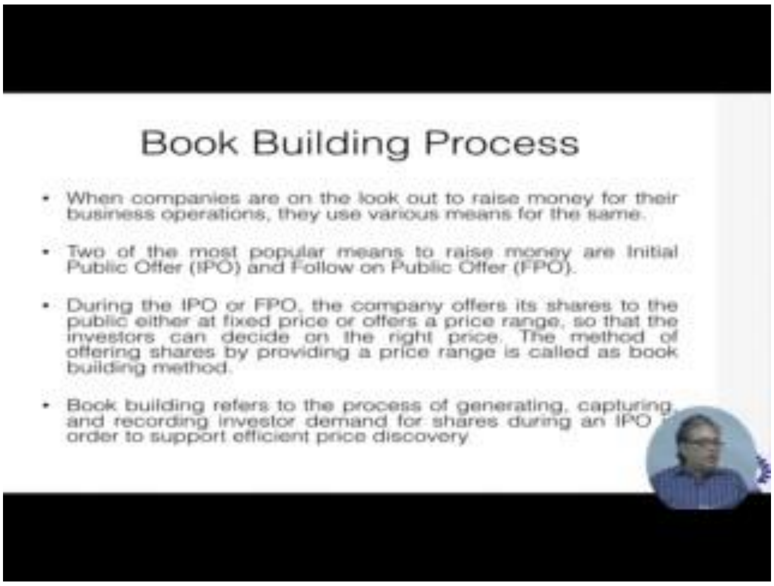

And at the same time you are required to give the information regarding the post issue capital structure that means, how much the promoters is going to hold in a post issue. Please remember, the promoters of this particular companies are need to hold 20 percent in the post issue capital that is the mandate and so when you are going for IPO, you might require to increase your stacking that company by the new subscription.

Now, I have talked with you the book building process few minutes back. The book building process is required to understand what should be the price or issuing price that means, how much premium should charge and there is a kind of a process which you need to follow and which I have listed into this particular slide itself.

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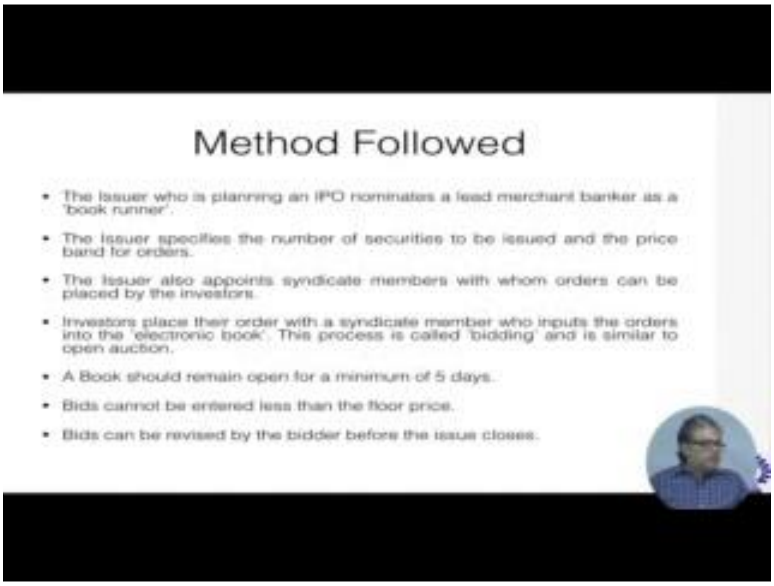

Now, these are the methods which you need to follow, you can go through this particular slide and it basically talk about that, what are the number of securities you are specified, then the minimum per days when the books will be remain open and then cannot enter the lesser than the floor price.

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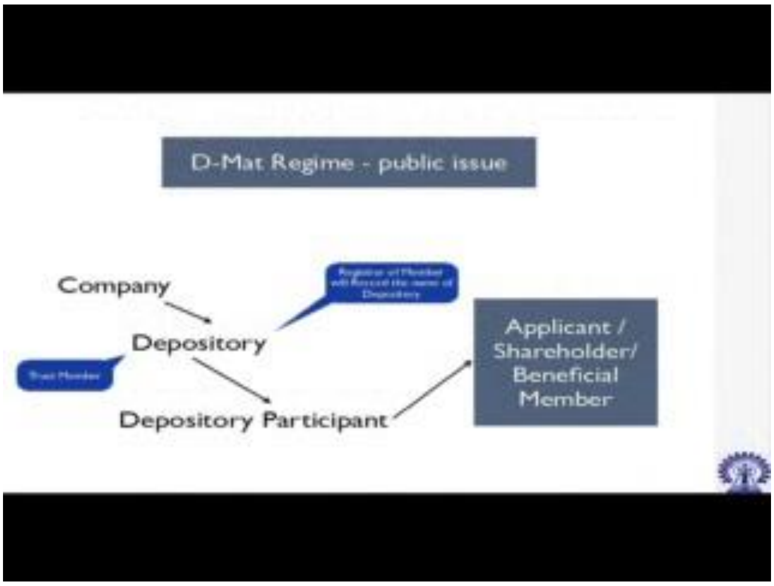

Now, let me talk with you relating to D-Mat or public issue because I have told you that D-Metallization one of the important aspect in nowadays because any public company, if they wanted to issue the shares or any other securities that has to be in the electronic form and if you look into this particular diagram, what I did, I have basically indicated that the company need to issue the shares to the depositories and depository registrar of member will record the name of this particular depository to whom it has been issued. Now, depositories again allocate this particular securities in the depository participant account, depository participants basically holds the account of the applicants whoever is applying for this particular security and they are going to allot this number of securities, the applicant is applied once their application is been scrutinize and they found eligible for this particular issue.

So, this has actually facilitated in transacting in the secondary market that means, in stock exchange study it is also facilitated in liquidating this particular securities and at the same time, this also helps for better transaction because it has reduced as security, I mean security instrument or losing of this particular security instrument, which is used to be in case of the physical form. So, this is all about relating to the procedures which you need to follow relating to the issues of instrument and this particular processes keeps on updating and subjected to changes.

So, you need to make your sub updated or you should take an advice from the professionals whenever you have decided to access the primary market and primary market is a very complex job. So, you only go to the primary market when you are confident that you have grown to that extent that you can really raise that particular money, the amount of money and at the same time let me tell you the accessing the primary market is very, very costly affair.

So, if you are not able to get a good premium against your security, going to the capital market or primary market is no good or further matter you are going to be lot of trust by going to the primary market. So, you should first find out the alternative source of finance which is available and if you think that your financial appetite is more and which cannot be fulfill by this particular alternative sources then only you should go to the primary market.

Thank you.