

PN-ACC-462

**Assistance to the Securities and
Exchange Board of India of
Certification, Licensing and
Testing of Capital Market
Intermediaries**

**Financial Institutions Reform and
Expansion (FIRE) Project**

January 1998

**Financial Institutions Reform and Expansion
(FIRE) Project
US Agency for International Development
(USAID/India)
Contract #386-0531-C-00-5010-00
Project #386-0531-3-30069**

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Price Waterhouse LLP



January 31, 1998

Mr Ashok Jha
United States Agency for International Development
B 28, Qutub Hotel Road
New Delhi 110 016

Dear Mr Jha,

**Re Broker Licensing, Testing and Certification Activities under the
Financial Institutions Reform and Expansion (FIRE) Project**

On January 16, 1998, as a further step towards the implementation of Licensing and Certification in the Indian Capital Markets, **the SEBI committee for Certification and Testing of Persons Joining Capital Market Intermediaries** has submitted its final report to Chairman, SEBI. The report is enclosed for your reference.

As you know, the PW/ FIRE Project funded by United States Agency for International Development (*USAID*), has been assisting the Securities and Exchange Board of India (*SEBI*), in implementing a Licensing, Testing and Certification program for intermediaries in the Indian capital market. The project has also provided 362 person weeks of training for 2215 persons through October 1997. Our observations follow.

Purpose of Activity

The Indian markets are going through a phase where there is a complete lack of faith from the Indian investors. The interface to the markets is through intermediaries functioning in the market. This segment needs to be organized and professionalized. To create and sustain investor faith the Indian markets need to find means of registration of those intermediaries that are unregistered and a program for licensing all intermediaries through testing and certification.

The purpose of this activity is to assist SEBI in the implementation of a program of licensing and testing for all market intermediaries.



Activities undertaken and accomplishments

SEBI established the “Committee for Certification and Testing of Persons Joining Capital Market Intermediaries” (*the Committee*) to consider all relevant issues and make recommendations on this subject

PW FIRE Project has been a permanent advisory member of the committee, principally represented by Mr Thomas Keyes, President, Securities Services International and Capital Markets Consultant to PW, and Mr Paritosh Sharma, Securities Markets Specialist

The PW consultants assisted the committee in all its deliberations, in understanding the Indian markets, understanding and evaluating the international practices and in finalizing its recommendations. PW further assisted the committee in writing a minimum criteria based examination syllabus and a consultative paper on the subject that was released by SEBI in January 1997

The following activities were completed by PW in assisting the committee in finalizing its report

- 1 PW provided significant input to SEBI on the issues involved in registration and regulation of retail capital market intermediaries and the testing and certification of these intermediaries. This input included the understanding of the Indian markets, the international experience as regards certification and testing, the choices and examination administration issues

a Registration of the retail market intermediary

The critical aspect that PW brought to the fore of the deliberations was the need to register and professionalize the retail market intermediary, the sub broker. Prior to PW intervention on this subject, this critical issue was assumed to have been solved by SEBI’s regulations for brokers and sub brokers. However, PW identified the specific groups of intermediaries who interact directly with the investors public and the role played by these groups. This group of intermediaries that is unrecognized in the Indian markets is the most critical segment of the retail market because it is the retail investor’s contact point with the capital markets. Therefore it needs to be registered and professionalized.



b Choices for registration- Industry Self Regulation

PW 's suggestions for the choices for the registration of retail intermediaries, including the most appropriate choice of self regulation by the industry were

presented to SEBI as well as the committee. The testing process can also be used as a means of registration. The committee has recommended an industry standing committee responsible for administering the exam which would be the first step towards creating an industry wide self regulatory organization on the lines of the National Association of Securities Dealers (NASD) of the US. The Indian equivalent is expected to register all intermediaries, test them and grant them licenses to be able to work in the industry, maintain informational and compliance databases of all intermediaries and effectively regulate them.

c Other financial intermediaries

PW also realized that for investor protection all financial intermediaries have to be included in the registration process. PW identified other intermediaries, such as merchant bank personnel investment advisers, and other asset managers who should be registered with SEBI.

2. PW developed a model syllabus based on minimum criteria and level of knowledge relevant to these groups and presented it to the committee.
3. PW proposed a model examination process including a question bank for these groups and test administration procedures.
4. PW assisted the committee in preparing the consultative paper on the issue that was released by SEBI for public comment. The consultative paper included the draft recommendations of the committee, the examination process and the model syllabus.
5. PW further assisted the committee in reviewing the comments received in response to the consultative paper.
6. PW then assisted the committee in finalizing the recommendations and its report to SEBI.



Deliverables Submitted

The following deliverables were submitted by PW/ FIRE to SEBI and the Committee

- **Design and Implementation of Licensing, Certification And Testing Program For Persons Joining Capital Markets Intermediaries**, Thomas Keyes, January 15, 1996
- **Design and Implementation of Licensing, Certification And Testing Program For Persons Joining Capital Markets Intermediaries**, Thomas Keyes, February 15, 1996
- **Certification and Testing of market intermediaries**, Mr Thomas Keyes, May 16, 1996
- **Registration and regulation of Retail Capital Market Intermediaries, The Sub Brokers**, Thomas Keyes, October 15, 1996
- **Registration And Regulation Of Retail Capital Market Intermediaries, The Sub Brokers**, Thomas Keyes, April 1997
- **Assistance to SEBI - Report on Financial Responsibility Framework**, Harry Melamad, April 1997
- **Registration And Regulation Of Retail Capital Market Intermediaries, The Sub Brokers**, Thomas Keyes, May 1997
- **Certification and Testing of Persons Joining Capital Markets Intermediaries**, Thomas Keyes, May 1997

Training

- **An Orientation Program On The US Model For Regulation And Registration Of Retail Capital Market Intermediaries For SEBI** Thomas Keyes and Paul Litteau, September 1996
- **An Orientation Program On International Capital Markets For Ministry Of Finance, SEBI & The Stock Exchange, Mumbai**, Thomas Keyes And Paul Litteau, November 1996



Completed In- Country Training Till October 1997					
No of persons	Home Organization	Program Length	Person Weeks	Timing	Workshop/ Seminar/ Instructor
8	SEBI	1 day	2 pw	Dec 1995	<i>Licensing and Certification Tom Keyes</i>
5	UTI Institute of Capital Markets	1 day	1 pw	Dec 1995	<i>Licensing and Certification Tom Keyes</i>
75	Madras Sub brokers	1 day	15 pw	April 1996	<i>Sub Broker Workshop Tom Keyes</i>
50	Calcutta	1 day	10 pw	May 1996	<i>Sub Broker Workshop Dennis Grubb/ Paritosh Sharma</i>
705 at 4 centers	SEBI/ Broker Certification	½ day each	70 5 pw	Sept 1996	<i>Sub Broker Workshop Bombay/ Delhi Tom Keyes</i>
125	Individual Investors	½ day	12 5 pw	Oct 1996	<i>Recent developments in the Capital Markets Tom Keyes</i>
1330	Regional Tour	1 day	266 pw	Jan 2-20, 1997	<i>Future of the Sub broker Tom Keyes / Paritosh Sharma</i>
25	SEBI/ NSE/ BSE/ OTCEI	2 days	10 pw	Jan 23-24, 1997	<i>Broker Dealer Financial Responsibility Paul Litteau/ Harry Melamad</i>
30	BSE	0 5 day	3 pw	June 25, 1997	<i>Securities Markets Tom Keyes and Paritosh Sharma</i>
2215	Total		362		

Future Activities

PW is carrying on with its efforts to further the above objectives of registering all intermediaries in the industry and licensing them through a testing process To this end PW FIRE Project shall continue the following

- Support SEBI registration databases for intermediaries such as merchant banks, investment advisors and asset managers (1998)
- Present a deliverable to SEBI which proposes a liquid net capital rule, record keeping rules, ethical standards/ code of conduct, disciplinary and dispute resolution procedures, and alternate regulation approaches for these retail intermediaries (May 1998)

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- Assist forums on investor protection in conjunction with Indian associations (January - August 1998)
- Assist in enhancing SEBI regulation to provide for registration of other intermediaries such as investment bankers not holding customer assets (By August 1998)
- Present a deliverable that would provide methods of arbitration, handling of broker insolvency, determination of appropriate selling practices and operations and regulations for private placements etc (By August 1998)

Thanking you

Sincerely,

W Dennis Grubb
Principal Consultant

*Assistance to the Securities and Exchange Board of India
on Certification, Licensing and Testing of
Capital Market Intermediaries*

*Price Waterhouse LLP
Mumbai
January 1998*

REPORT
OF
THE COMMITTEE
FOR
CERTIFICATION AND TESTING
OF
PERSONS JOINING
CAPITAL MARKET INTERMEDIARIES

*Securities and Exchange Board of India,
Primary Market Department
January, 1998, Mumbai*

Acknowledgments

The Committee wishes to acknowledge the contributions of all those who participated in discussions of the Committee

*Mr Thomas R Keyes, Capital Market Consultant, Price Waterhouse
Mr Paritosh Sharma, Securities Markets Specialist, Price Waterhouse and
Mr Vivek Kulkarni, Deputy General Manager, Credit Rating and Information
Services of India Limited (CRISIL),
for their invaluable assistance throughout the duration of this Committee*

The Committee also wishes to thank Dr G Sethu of the UTI Institute of Capital Markets (UTI ICM) for his assistance in finalising the syllabus and the Director, Faculty and other members of the staff of the Institute of Banking Personnel Selection (IBPS)

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INTRODUCTION

Investor Protection forms the central ethos of SEBI. Development and Regulation of Capital Market, the other objectives of SEBI, have at their root this very basic principle of investor protection.

Investor confidence is essentially a function of investor protection. The better the levels of protection, the more the confidence. Further, both investor protection and confidence can be measured by the faith that the investors have in systems and processes of the capital market.

Intermediation, the basic process in the capital markets, includes proper understanding of the various facets of the securities market so as to provide fair and competent advice to investors. It is, therefore, felt that improvement in the quality of intermediation will go a long way in achieving the objective of investor protection. As intermediation involves human capabilities and calibre more than technological support, it is important that any person appointed in any position with an intermediary institution which has investor interface or those who are self employed in the industry have the necessary professional standard.

The desirability of such professional standards is further highlighted by the transformation that the capital market of the country is witnessing

1. Increasing integration with the capital markets of other countries. In other words, the insulation that the Indian capital market enjoyed till recently, from the events taking place in other economies is disappearing.
2. Increasing dependence of the corporate sector on capital market which is emphasised by the fact that Banks (both Public and Private) and lately Municipal Corporations have been planning to enter the capital market to raise funds from the public. The Government has also decided to disinvest its stake in the Public Sector Units through offers for sale.
3. Increasing integration of the capital market with the forex market. The last few months have seen the turmoil in exchange rates affect the movement in the stock market indices.
4. Increasing automation and institutionalisation of the capital markets, along with an increasing sophistication in capital market operations.

with the advent of screen based trading, depositories, book building, etc

☐ Increasing level of awareness among investors

This transformation can be sustained only by ensuring that well qualified and trained personnel, who are willing to continuously update their skills enter the securities industry to assist investors. The industry is in a continuous state of change with new skills being required for the functional areas. For instance, the business of stock broking is radically different now from what it was in the past. A stock broker learned the intricacies of the business through family traditions or through working with a stock broker. However, in the fast changing scenario of today, such traditional learning of skills may not be enough and there is a need for professional and specialised knowledge for the persons already working in the industry and also for those who are desirous of entering the industry.

There is a large work force engaged in the capital market with varying levels of professional qualifications, skills and experience. The persons working in the industry should realise the responsibility they shoulder and must be aware of the consequences their acts of omission and commission have on investors. It is essential that they are well equipped to play their designated role in the securities industry. While some of these persons may have the desired levels of professional standards, a large portion is acutely deficient. Moreover, there are a variety of functions in the securities industry that need different levels and nature of specialisation and orientation. Therefore there is a need to match the professional standards of those who are in the market with the functions they perform.

While there are no standards of qualifications for employment in the industry, the preferred qualifications are M B A , C A , C S , M Com , etc. Skills are learned on the job and presently there is no formal education or training on capital markets especially in the area of operations, except some short term courses and seminars conducted by some institutions. Therefore, the industry needs to have a system of that would ensure minimum standards for industry participants and thus enhance professionalism in the capital market.

New exchange members need to fulfill certain basic requirements to be eligible for admission as members of any stock exchange. These are provided under the Securities Contracts (Regulation) Rules, 1957 and SEBI (Stock Brokers and Sub Brokers) Rules and Regulations, 1992. Further, the Ministry of Finance, at the instance of SEBI, in November 1989 prescribed authorisation criteria and a uniform selection process to be followed by all

REPORT OF THE SEBI COMMITTEE FOR CERTIFICATION

stock exchanges for admission of new members. The new member authorisation criteria consists of educational qualification, experience, financial solvency and interview performance. SEBI subsequently decided that the candidates should undergo a written test which should also form part of the selection process for new members. New exchange members are the only industry participants who are required to go through a qualification examination.

This process of ensuring a minimum standard is already established in most of the developed markets and is being introduced in the emerging markets around the world. The United States started this process in the late 1950s with a single test. As the testing process developed over time, tests were adjusted to the requirements of the market, which was gradually becoming more complex, to match the level of knowledge and skill required for the securities industry for specific market areas and for different functional levels. For example, the US now has twenty two separate securities tests for supervisors and sales people. The United Kingdom started with one test in the mid 1980s, and now has testing and certification for various market professionals. Other countries like Zambia and Indonesia etc have begun certification either by testing or through specialised courses followed by testing. Countries like Sri Lanka, Tanzania, Lithuania etc, have also initiated this process to improve the quality of their markets.

Taking into account the international experience and the needs of the Indian markets, SEBI considered Certification by examination for persons operating in the markets by one single test to begin with.

The Committee released a consultative paper in January 1997, presenting the views of the Committee on the various relevant issues. Comments were received from several organisations, institutions and individuals. The Committee obtained the comments of the market participants, investor associations, professionals etc on the various issues before finalising its report. The Committee places on record its appreciation for all those who responded to the consultative paper.

THE COMMITTEE FOR CERTIFICATION

With a view to improve investor protection through better quality intermediation, Chairman, Securities and Exchange Board of India set up a Committee, to lay down standards of certification for persons operating in the capital market. The following were nominated on the Committee

Shri Vijay Ranjan, Executive Director, Securities and Exchange Board of India, Chairman

Shri N J Yasaswy, Institute of Chartered Financial Analysts of India - Member

Dr Thiripal Raju, UTI Institute of Capital Markets - Member

Shri Uday S Kotak, Kotak Mahindra Finance Company Ltd - Member

Shri Ajit Day, Member, Calcutta Stock Exchange - Member

Shri K N Atmaraman, Tata Asset Management Company Ltd - Member

Shri Vivek Kulkarni, Division Chief, Securities and Exchange Board of India - Member Secretary

Ms Ruchi Chojer, Officer, Securities and Exchange Board of India [after Shri Vivek Kulkarni's proceeding to CRISIL on deputation]

THE OBJECTIVES OF THE COMMITTEE

The Terms of Reference of the Committee was to prescribe in general the standard of knowledge necessary for different types of specialised functions in the security industry at operational and supervisory levels. The Committee was also to outline the eligibility criteria for the candidates, testing process and other administrative details related to the proposed process.

The Committee was specifically required to look into the following

- 1 To identify a process by which general standard would be raised
- 2 To identify the eligibility criteria for applicants for the testing process
- 3 Any exemptions from the requirements of taking the testing process
- 4 To prepare the syllabus and design the testing process
- 5 To oversee the preparation of the study material
- 6 To recognise the institution/s that could conduct the tests
- 7 To lay down the procedures for award of certificates
- 8 To define the code of conduct for those who qualify
- 9 To decide on continuous testing criteria for updation of skills
- 10 To set up procedures for updation of examination, if required

ANALYSIS OF ISSUES AND RECOMMENDATIONS

The Committee met on several occasions and identified issues that needed to be focused upon. These issues were listed based on the existing qualification standards of the Indian capital market intermediaries, prevalent certification systems in the international capital markets and the current and future needs of the Indian capital markets. These issues were discussed with the objective of developing a suitable model for the Indian market which would be in line with international standards.

After due deliberations, **the Committee decided that an examination based certification system is ideal to meet the needs of the Indian capital markets.** Given below are the essential features of this system, the issues listed and discussed by the Committee and the recommendations of the Committee.

1.0 Essential Features of the Certification Programme

1.1 Certification Voluntary or Mandatory

During the deliberations of the Committee, it was felt that there is a need to establish a basic minimum standard for all persons operating in the industry. However, the Committee felt that this should be pursued as a longer term objective and to begin with such certification should be accepted by the market as a value addition to their quality of intermediation, thus making the testing process voluntarily acceptable. Voluntary testing initially would also ensure that the quality and standard of the test shall be designed to attract industry participants.

However, the Committee was firmly of the opinion that **though the test should be voluntary to begin with, considering the importance of developing and maintaining a minimum acceptable standard of intermediation, it should be made a mandatory requirement for operating in the industry, from an appropriate future date.**

The Committee recommends that,

- **the test be offered on a voluntary basis in the initial period and the test be so designed that the market perceives value addition in the quality of intermediation**
- **the test be made a mandatory requirement after a period of two years from the date of the first test**

1 2 Rules regarding mandatory testing

The Committee discussed at length about the possibility of making all the staff employed with intermediaries take the test, and considered the expected response from the market, the hardship for persons already operating in the industry on the date of implementation of mandatory testing and the administrative issues in conducting a test for a large number of people

The Committee also discussed the course curricula of professional examinations and the skill requirements of market intermediaries with reference to the knowledge of operations and procedures of the securities market

The Committee recommends that after the date on which this test becomes mandatory,

- **every person regardless of the qualifications they possess shall be required to pass the certification test prior to seeking employment with a capital market intermediary, subject to the conditions laid down below**
 - ♦ **no person shall be employed by a capital market intermediary unless he / she has passed the certification test or passes the certification test within a period of 12 months from the date of employment**
 - ♦ **two persons or 20% of the existing staff, whichever is higher, employed with the capital market intermediary shall have to obtain the certificate within 12 months from the date on which the test becomes mandatory**
 - ♦ **any person who has not been active in the securities markets i e who has not been employed with a market intermediary or who has not been self employed in the industry, for a period of two years or more, shall be required to pass the certification test, within a period of 12 months from the date of reemployment**

1 3 Exemptions

The Committee considered testing for intermediaries that have been active in the securities industry and felt that due to the fast pace of development in the Indian capital markets even these persons need to upgrade their skills and the test shall add value to them It was also felt that even though

certain exemptions may be necessary keeping in view the Indian market conditions, these exemptions should be minimal

The Committee recommends that, exemption from the requirement of mandatory testing be granted only to those persons who have attained the age of 50 years on the date when the test becomes mandatory and have an experience of at least 10 years in the capital market at that time, being employed with a SEBI registered capital market intermediary

1.4 Single or Multiple Testing

The Committee, in its deliberations, felt that the securities industry has different specialisations which require different levels and nature of skills and knowledge for different participants. For example, an employee of a merchant banker requires different skills than an employee of a registrar or a broker. Each intermediary takes decisions regarding suitability, while selecting employees for different specialised functions. However, in the absence of any minimum criteria test, as is being proposed now, the intermediary does not have an assured minimum level of skill or knowledge of the prospective employees to choose from. In this context, therefore, the Committee felt that each of these functional segments, should be tested separately for their respective skills and the required levels of knowledge.

However, the Committee agreed that such specialised multiple testing should be a long term objective, after the concept of testing and the attendant benefits to market players are widely accepted.

Therefore, the Committee recommends that,

- **the certification exam system be introduced with a single common test for all market intermediaries**
- **specialised tests should be introduced for different market participants at a later date as required by the market conditions**
- **the Self Regulatory Organisations, if any, of the specific market segments for which specialised testing is to be introduced, be involved by SEBI in developing the syllabus at the time such specialised testing is introduced**

1 5 Period of Validity

The Committee recommends that the certificate will be valid for life and the candidate will not be expected to take the test again, as long as he/ she is active in the securities industry. The term 'active' shall mean that the person after obtaining the certificate at any time has not been inactive for a period of two years.

However, the Committee felt that with the introduction of new functional areas in the securities industry specialised skills would need to be developed by market participants employed in these areas.

The Committee recommends that SEBI should prescribe specialised tests as a precondition for intermediaries operating in new markets and in new products such as derivatives, etc , at a later date.

1 6 Action in case of non compliance

The Committee feels that it is important that SEBI form and implement penalty measures for non compliance with the testing requirements.

The Committee recommends, therefore, that the intermediary that violates the minimum number of certified employees norm shall be deregistered from the date of the said violation.

1 7 Syllabus

The Certification test is intended to safeguard the investing public by ensuring that the intermediaries they are dealing with are competent to perform their functions. The examination will seek to measure whether a candidate possesses the requisite knowledge and skills to competently perform the critical functions.

Critical functions performed by intermediaries in their dealing with the investing public were identified and deliberated upon by the Committee. Proceeding from its deliberations, the Committee identified the specific areas, the knowledge in which was considered essential to perform each critical function competently.

The syllabus for the test and the test process have been formulated keeping in mind the educational level and the functions performed by the intermediaries. The syllabus therefore, should prove useful as a means of understanding the purpose and nature of the exam and an introduction and guide to the basic subjects tested by the exam.

The test will cover relevant areas so that the intermediaries are able to assess the investors risk profile, suggest a menu of investment choices, help the investor with the paper work, appraise them of their rights and guide them in remedying their investment problems

The committee recommends a syllabus that has seven sections broadly categorised as Investor Profile, Investment Products, Investment Math, Investment Procedures, Rules & Regulations, Investor Protection, Ethics & Codes of Conduct. The syllabus is attached to this document as Appendix A.

1.8 Eligibility

The Committee felt that persons should be encouraged to augment and supplement their knowledge through the test without concern for their educational or occupational qualifications. Therefore, the Committee after its deliberations proposed that there is no need to prescribe any pre qualification eligibility requirements

The Committee recommends that the examination can be taken by anyone, irrespective of qualifications, age, employment or experience. However, the syllabus and the examination have been designed for candidates with at least 12 years of schooling

2.0 Administrative Structure

The Committee for Certification recommends the following administrative structure for efficient implementation of the proposed examination based certification system

2.1 Standing Committee

The Committee recommends that a Standing Committee may be formed to take further decisions for enhancing professional standards in the securities industry

Functions

The functions of the Standing Committee should include the following

- periodically reviewing
 - ◆ the syllabus,
 - ◆ testing standards,
 - ◆ the examination patterns

- ♦ the test administration and
- sponsoring and developing a Self Regulatory body to take over the role of the Committee

The Constitution

The Standing Committee may be appointed by Chairman, Securities and Exchange Board of India. Persons with highest standards of professional achievement in public, private, or academic sector may be appointed

- The Standing Committee should be broad based with representation from different regions, stock exchanges and intermediaries. While constituting the Committee, fair representation should be given to intermediaries, academic researchers, investor representatives and professional bodies
- Initially the Committee may have 3 members from amongst intermediaries, 2 researchers, one investor representative and two representatives from the professional bodies
- Rules should be created that would allow that the members be removed for any professional misconduct, with two thirds of the Committee approving the removal
- A suitable officer of SEBI should be appointed as Chairman and secretarial assistance be provided by SEBI
- The Committee may co-opt any person for specific meetings. The co-opted members should have no right to vote, but their views should be recorded in the minutes

2.2 Examination Committee

The Committee also recommends that an Examination Committee be formed by SEBI

Functions

The examination Committee shall be responsible for the following functions

- maintaining an exhaustive question bank,

- updating lists of professors of reputed business schools and senior executives of reputed intermediaries who will participate in setting questions,
- deciding the weightage for each section and reviewing the syllabus,
- reviewing the performance of the specialised agency appointed to administer the test and proposing changes if necessary

This Committee must function as an autonomous body and should not be a sub-committee of the Standing Committee

The Constitution

- The Examination Committee may be constituted out of the Standing Committee with some additional members
- This Committee should be appointed for specified periods
- The Committee may have five members, two professors of prestigious management schools, two intermediaries and one regulator
- The Committee should maintain the highest standards of professional integrity

2 3 Secretariat

Chairman, SEBI may appoint a suitable officer and a secretary to provide the secretarial assistance to the Committee. The Secretariat will be responsible to process all the administrative work related to the examination.

3.0 Essential features of the test

3 1 Structure

The Committee feels the test should examine the entry level knowledge of selected functions based on the minimum criteria required for entering the securities industry. The Committee also feels that the emphasis in the proposed test should be on basic concepts rather than memory testing.

Therefore, the Committee recommends that,

- **a multiple choice test should be offered**

- **the minimum passing score may be kept at 70% However, the weightage for each section shall be notified in advance for the benefit of the candidates**
- **the test can initially be administered in cities with stock exchanges**

3 2 Standard

The Committee felt that the standard of the test has to be sufficiently high for the applicants and the employers to feel that the test adds value. At the same time the test should be based on the minimum criteria that a person employed in the industry needs to have. This balance is essential for the success of the test.

The process of maintaining the quality of the test should be continued even after the first test has been administered as experience is gathered in the area.

The Committee feels that the Examination Committee should formulate the test, taking into account the need to maintain sufficiently high standards

3 3 Administration

The test is best administered by a specialised agency. The Committee considered the ability of the Institute of Banking Personnel Selection, Mumbai for the purpose of administering the test. In the opinion of the Committee the institute has the right infrastructure to handle all aspects of test administration. They administer the IIM entrance exam as well as the State Bank of India probationary officers exam. They have several other public and private sector clients. In the recent SBI probationary officers entrance exam, the institute handled 3.5 lakh applicants. The institute has 12 faculty members specialised in psychometric analysis. The institute has a capacity to handle all aspects of test administration including co-ordination with the Examination Committee, maintaining a question bank, generating a random question paper, printing the test booklets, processing the applications, conducting exams all over India, tabulating and declaring results and maintaining the data base of both applied and successful candidates. The institute is willing to participate in the proposed activity.

Though the final decision on the agency lies with the Standing Committee, this Committee recommends that the Institute of

Banking Personnel Selection, Mumbai, may be used to conduct the proposed test

3 4 Frequency

The Committee recommends that,

- the tests should be conducted twice a year, at an approximate frequency of six months
- the frequency of the test can be increased, depending on the response from the market and the number of applicant candidates

3 5 Application form

Information to be collected

The Committee recommends that, the application form should require applicants to provide all relevant information about their educational background and experience as well as information that would confirm the identity of the applicant

Penalty for false information

The Committee also recommends that, SEBI shall impose penalty of decertification for those persons who provide false information in the application form

3 6 Finance

The certification work should eventually pass on to a Self Regulatory body and therefore the project has to be self financing. The main source of revenue would be the examination fee

The fees should be sufficient to create and maintain a high standard of testing and administering the exam

The Committee has proposed a system which would require keeping of records of successful candidates on a continuous basis as opposed to the other tests which are one time tests and the records of successful candidates are not kept after the process of testing is over for the year

Also, the preparation of a challenging question bank for this test would be a costly exercise. The other tests like the IIMs, banking entrance etc are aptitude tests where a number of questions can be offered without much repetition. The certification test questions are expected to be more difficult to set as the questions have to be restricted to the specialised functions as defined by the testing criteria. The services of professionals from premier institutes and also of reputed private consultants are required which will make the test preparation more expensive.

In view of these reasons the Committee recommends that an examination fee of Rs 1500/- be charged from the applicants

4.0 Issue of Certificates

The Committee recommends that,

- **each successful candidate should receive a certificate signed by the Chairman of the Examination Committee and the member secretary**
- **this certificate should have a unique number that shall be used by the Committee to maintain the database of certified candidates on a permanent basis**

Sd/-
Shri Ajit Day

Sd/-
Shri N J Yasaswy

Sd/-
Shri K N Atmaraman

Sd/-
Shri Uday S Kotak

Sd/-
Dr M Thiripal Raju

Sd/-
Shri Vijay Ranjan

SUMMARY OF RECOMMENDATIONS

1.0 Essential Features of the Certification Programme

1.1 Certification Voluntary or Mandatory

The Committee recommends that,

- the test be offered on a voluntary basis in the initial period and the test be so designed that the market perceives value addition in the quality of intermediation
- that the test be made a mandatory requirement after a period of two years from the date of the first test

1.2 Rules regarding mandatory testing

The Committee recommends that after the date on which this test becomes mandatory,

- every person regardless of the qualifications they possess should be required to pass the certification test prior to seeking employment with a capital market intermediary, subject to the conditions laid down below
 - no person shall be employed by a capital market intermediary unless he / she has passed the certification test or passes the certification test within a period of 12 months from the date of employment
 - two persons or 20% of the existing staff, whichever is higher employed with the capital market intermediary shall have to obtain the certificate within 12 months from the date on which the test becomes mandatory
 - any person who has not been active in the securities markets i.e. who has not been employed with a market intermediary or who has not been self employed in the industry, for a period of two years or more, shall be required to pass the certification test within a period of 12 months from the reemployment

1.3 Exemptions

The Committee recommends that exemption from the requirement of mandatory testing be granted only to those persons who have attained the age of 50 years on the date when the test becomes mandatory and have an experience of at least 10 years in the capital market at that time, being employed with a SEBI registered capital market intermediary

1.4 Single or Multiple Testing

The Committee recommends that,

- the certification exam system be introduced, with a single common test for all market intermediaries
- specialised tests should be introduced for different market participants at a later date, as required by the market conditions
- the Self Regulatory Organisations if any of the specific market segments for which specialised testing is proposed to be introduced, be involved by SEBI in developing the syllabus at the time such specialised testing is introduced

1.5 Period of Validity

The Committee recommends that the certificate will be valid for life and the candidate will not be expected to take the test again, as long as he/ she is active in the securities industry. The term 'active' shall mean that the person after obtaining the certificate at any time has not been inactive for a period of two years

The Committee recommends that SEBI should prescribe specialised tests as a precondition for intermediaries operating in new markets and in new products such as derivatives, etc, at a later date

1.6 Action in case of non compliance

The Committee recommends that the intermediary that violates the minimum number of certified employees norm should be deemed to be automatically deregistered from the date of the said violation

1 7 Syllabus

The committee recommends a syllabus that has seven sections broadly categorised as Investor Profile, Investment Products, Investment Math, Investment Procedures, Rules & Regulations, Investor Protection, Ethics & Codes of Conduct. The syllabus is attached to this document as annexure A.

1 8 Eligibility

The Committee recommends that the examination can be taken by anyone, irrespective of qualifications, age, employment or experience. However, the syllabus and the examination have been designed for candidates with at least 12 years of schooling.

2.0 Administrative Structure

The Committee for Certification recommends the following administrative structure for efficient implementation of the proposed examination based certification system.

2 1 Standing Committee

The Committee recommends that a Standing Committee may be formed to take further decisions for enhancing professional standards in the securities industry.

Functions

The functions of this committee should include the following:

- periodically reviewing
 - ◆ the syllabus,
 - ◆ testing standards,
 - ◆ the examination patterns,
 - ◆ the test administration, and
- sponsoring and developing a Self Regulatory body to take over the role of the committee.

The Constitution

The Standing Committee may be appointed by Chairman Securities and Exchange Board of India. Persons with highest standards of professional achievement in public, private, or academic sector may be appointed.

- The Standing Committee should be broad based with representation from different regions, stock exchanges and intermediaries.
- While constituting the committee, fair representation should be given to intermediaries, academic researchers, investor representatives and professional bodies.
- Initially the Committee may have 3 members from amongst intermediaries, 2 researchers, one investor representative and two representatives from the professional bodies.
- Rules should be created that would allow that the members could be removed for any professional misconduct, with two thirds of the committee approving the removal.
- A suitable officer of SEBI should be appointed as Chairman and secretarial assistance be provided by SEBI.
- The committee may co-opt any person for specific meetings. The co-opted members should have no right to vote, but their views should be recorded in the minutes.

2.2 Examination Committee

The Committee also recommends that an Examination Committee be formed by SEBI.

Functions

The Examination Committee shall be responsible for the following functions:

- maintaining an exhaustive question bank,
- updating lists of professors of reputed business schools and senior executives of reputed intermediaries who will participate in setting questions,
- deciding the weightage for each section and reviewing the syllabus.

- reviewing the performance of the specialised agency appointed to administer the test and proposing changes if necessary

This committee must function as an autonomous body and should not be a sub-committee of the Standing Committee

The Constitution

- The Examination Committee may be constituted out of the Standing Committee or with additional members
- This committee should be appointed for specified periods
- This committee may have five members, two professors of prestigious management schools, two intermediaries and one regulator
- The committee should maintain the highest standards of professional integrity

2 3 Secretariat

Chairman, SEBI may appoint a suitable officer and a secretary to provide the secretarial assistance to the committee. The Secretariat will be responsible to process all the administrative work related to the examination.

3.0 Essential features of the test

3 1 Structure

The Committee recommends that a multiple choice test should be offered.

The Committee also recommends that the minimum passing score may be kept at 70%. However, the weightage for each section shall be notified in advance for the benefit of the candidates.

The test can initially be administered in cities with stock exchanges.

3 2 Standard

The Committee feels that the Examination Committee should form the test taking into account the need to maintain sufficiently high standards

3 3 Administration

Though the final decision on the agency lies with the Standing Committee, this Committee recommends that the Institute of Banking Personnel Selection, Mumbai, may be used to conduct the proposed test

3 4 Frequency

The Committee recommends that the tests should be conducted bi annually at an approximate frequency of six months

3 5 Application form

Information to be collected

The Committee recommends that the application form should ask for all relevant information about the candidates educational background and experience as well as information that would confirm the identity of the applicant

Penalty for false information

The Committee also recommends that SEBI should impose penalty of decertification for those persons who provide false information in the application form

3 6 Finance

The Committee recommends that an examination fee of Rs 1500/- be charged from the applicants

4.0 Issue of Certificates

The Committee recommends that each successful candidate should receive a certificate signed by the Chairman of the Examinations Committee and the member secretary

REPORT OF THE SEBI COMMITTEE FOR CERTIFICATION

The Committee also recommends that this certificate should have a unique number that shall be used by the Committee to maintain the database of certified candidates on a permanent basis

APPENDIX

Draft Syllabus for Certification Test

*The Report of the Committee for Certification
of Intermediaries in the Capital Market*

*Securities and Exchange Board of India,
Primary Market Department
January, 1998, Mumbai*

SECTION I INVESTOR PROFILE

The purpose of this section is to introduce elementary techniques to determine the investors profile. The profile would contain the investors basic family information, income, present portfolio and risk tolerance. Based on a simple questionnaire the investors risk taking ability would be assessed. Appropriate class of investments would then be recommended to the investor. The section provides details on obtaining customers, appropriate communications, investor information, risk profile in the following paragraphs

Obtaining Investors, Communications to Investors, General standards of truthfulness and good taste, Recommendations of securities, disclosure of current price, market making, other relevant information, Authentication of communications, Ethics and Code of Conduct that govern solicitations, investment advice and advertisements

Obtaining Investor information, An advisor (Broker, Sub-broker, Portfolio Manager) should take reasonable steps to ascertain details covering the investor risk profile, financial profile, social profile investor identification details, family income, employment, age, investments, other assets, financial liabilities, other responsibilities, social standing, investment horizon, risk taking ability etc

Investment Product Risk classification Different products have different degrees of risks. An understanding of these is required for providing the best advice to the investor. Fixed Income Investments (Government (Public Sector) and Private Sector), Tax Oriented Investments, Growth Investments, Speculative Investments

Providing Best Advice to the Investor, In line with investor needs. Should not make any specific recommendation without determining suitability for the investor, should inform relevant facts to investor before investing, to be satisfied that no other better investment opportunity is available

Investor agreement

Best Execution of Orders (best price, best advantage to investor)

SECTION II INVESTMENT PRODUCTS

The purpose of this section is to introduce an array of investment products that range

from risk free government securities, corporate debentures, stocks to speculative investments like plantation schemes. The products are primarily classified into Fixed Income, Mutual Funds, Shares and Speculative Investments. The risk return trade off of each investment is also explored. The information presented in this section will help the applicant in recommending the right investment for an investor. This recommendation will of course depend on the investors risk profile which was explored in Section I.

Fixed Income Investment products Bank deposits, Central Government Securities, State Government Securities, Bonds issued by Local Authorities, Relief Bonds, Indira Vikas Patra, Public sector bonds, Cumulative Term deposits (CTD), Treasury bills, Commercial Paper, Bill of Exchange (hundı), Certificates of Deposits, National Savings Certificates (NSC), Public Provident Fund, National Savings Schemes, Retirement benefit plans, Post office small savings scheme, Company Debentures, Company fixed deposits, Deep Discount Bonds, Secured Premium Notes, Floating Rate Note (FRN), Zero Coupon Bond, Zero-Coupon Convertible Bond, STRIPS

Features of fixed income products Amount of Investment, Face Value / Par Value / Issue Price, Periodicity, Cumulative and/or Non-Cumulative, Maturity, Denomination, Interest Rate / Discount / Yield, Safety, Credit Rating, Secured / Unsecured, Convertible / Non-convertible, Put and Call Options, Conversion Time/s, Conversion Price, Premium, Front-end Discount, Interest Payment Periods, Redemption / Withdrawal Terms, Premature Withdrawal Terms, Loan availability, Taxation, Persons eligible to Invest etc

Mutual Funds Types and features, Asset Management Company's Offering Funds (AMCs), Close-end funds, Open-end funds, Growth funds, Income funds, Balanced funds, Index funds, Money market mutual funds, Equity Linked Tax Saving Schemes (ELSS), Sectoral fund, Off-shore fund/country funds, Speciality funds, Small companies funds, International funds, US 64 etc

Shares Preference shares, Equity Shares, *Warrants* - Exercise price, time limit number of shares / bonds per warrant, price of warrant, detachable warrants, attached warrants, puttable warrants, naked warrants, *Rights on equity shares* - Rights Ratio, Rights Price, Price of underlying Assets, Ex-rights price, Cum-rights price, Book Closure, *Global Depository Receipts (GDRs)*, *American Depository Receipts (ADRs)*

Speculative Investments This section introduces several leveraged instruments

Readers are expected to know elementary details

Futures Financial futures, standardized, cash price, futures price, contract time, delivery date, *Options* Call option, put option, strike price, buyer, option writer, Greenfield venture schemes in *plantations, real estate* investments

Risk Security specific, business, interest rate, inflation, exchange rate, political, liquidity and credit risk, risk free rate of return, market rate of return, risk premium, risk return trade off of investment products, elementary principles and advantages of diversification

SECTION III INVESTMENT MATHEMATICS

This section deals with basic concepts and quantitative tools, helpful in the understanding and interpretation of investment information available from the financial press and financial product literature

Terminology

Bonds and Debentures Simple yield, current yield, yield to maturity, redemption yield, coupon rate, principal, face value, maturity, discount, premium, simple interest, compound interest, quarterly compounding, semi annual compounding, duration, conversion premium

Equity Shares Share price quotation, return on equity investment, earning per share, dividend yield, cash earning per share, price to earning ratio (earnings multiple), diluted P/E, adjusted EPS, fully diluted EPS, book value, market price, intrinsic value, dividend yield, capital gain, value of a 'right', value of 'bonus', capitalization rate, cost of equity, cum dividend price, ex dividend price, initial public offering, offer price, beta

Time Value Present value, future value, compound value, annuities, amortization, discount rate, internal rate of return, equal monthly instalments

Stock Exchange Indices Names of important indices, composition of indices, differences between various indices, basic application of indices

Mutual Funds Amortization of front end fees, net asset value, discount/ premium to NAV, impact of loading on returns

Warrants, Futures, Options, Swaps, GDRs, ADRs, ECBs, Rights Exercise price of a warrant, time limit, naked warrants, puttable warrants, cash price of a future, futures price, cost of carry, contract time, delivery date, call option, put option, exercise price of an option, option premium, intrinsic value of an option, in the money option, out of the money option, option writer, option holder, interest rate swaps, currency swaps, fixed rate, floating rate, maturity of a swap, swap payment, issue price of a GDR/ADR, GDR Ratio, premium/ discount of a GDR/ADR, underlying asset in a GDR/ ADR/ derivative, rights ratio, rights price, ex rights price, cum rights price, rights closure, bonus closure

Financial Statements Net worth, current assets, current liability, debt to equity ratio, current ratio, margin, turnover ratios, cost of capital

Taxation Personal Income Tax, Tax planning investments, pre tax return, post tax return

General libor, basis points, credit rating, inflation rate, real rate of interest, capital adequacy

Basic Investment calculations

Bonds, term loans and Debentures Simple and compound interest rate calculations, bond yield calculations, annuities and amortization, yield calculations, riskiness (credit risk, liquidity risk, interest rate risk, inflation risk), reading financial tables

Firm's equity related calculations EPS, cash EPS, book value, net worth, risk of the equity share, dividend yield, capital gain yield, earnings yield, adjustments for rights, bonus, conversion, dividends, premia and discounts

Mutual Funds Total market value, net asset value, offer price, sales charge

Calculations that help in interpretation of financial information Ratios in financial statements, simple financial analysis (time series, cross sectional), Du Pont chart common size income statement and balance sheet

Investment decision making Pay back period, internal rate of return, net present value, return on investment

Data Sources Annual reports of companies, stock exchange publications, CMIE

publications, RBI economic statistics, financial dailies, financial magazines, brochures, brokerage research publications, financial television programmes, data banks, newsletters, credit rating agency information, on line data sources (e.g Reuters, Bloomberg)

Data interpretation

Reading, understanding and interpreting financial statements brochures on new issues, newsletters to investors, interpretation of credit ratings, *Deficiencies in using documented information* on standardization of data and definitions, non adjustments for rights, dividends, bonus, non representative samples in data reporting, inappropriate comparisons (arising out of size effect, differences due to differing accounting policies, nature of business, non - coincidence of accounting periods, special considerations due to geographical locations of the firms, etc)

Misunderstanding of some financial indicators An illustrative list Economic worth of book value, Investment at cost, Valuation of fixed assets, Depreciation as a source of funds, Price Earnings ratio, Accounting earnings per share, Dividend yield as cost of capital, Auditor's qualifying remarks and the notes to accounts, estimates or projections in the prospectus have to be judged carefully

SECTION IV INVESTMENT PROCEDURES

This section deals with procedures and processes involved in securities investment While opening a bank account is simple, primary market issues and secondary market trading require an overall understanding of market practices This section describes in brief the market players and the institutional arrangements that go into the investment process

Primary market procedures Primary market procedures related to public issues and rights issues Instruments such as equity shares, preference shares, cumulative convertible preference shares, debentures, floating rate notes, warrants and so on are sold through the primary market mechanism

This involves *understanding procedures* like Obtaining the share application form and prospectus, contents of application, understanding the prospectus (short term, highlights, risk factors, projections, EPS, P/E ratio, promise vs performance, litigations, contingent liabilities etc), application money, stock invest, receipt of allotment advice/ refunds, proportionate allotment, listing

The role of intermediaries like registrars, banker to an issue, lead manger, merchant banker, investment adviser, custodian etc and *understanding related terms* like book building, net offer to public, promoters contribution, lock in shares, private placement, road show, grey market, IPOs, composite issue, credit rating, asset backed securities etc

Secondary market Procedures Stock Exchanges Role and Functioning, Membership, Brokers and sub brokers, Jobbers and market makers

Trading on own account, on behalf of investors, Trading hours, margins, Screen-based Trading Quote Handling, Order Handling, Order Execution, etc Bombay Stock Exchange (BOLT) Negotiable Deals, Crossed Deals, Opening price determination, Closing Price Computation, Touch line etc , National Stock Exchange (NEAT) Order Matching, Counter party exposure limits, Order types, Types of Conditions, Time Conditions, Price Conditions, OTCEI market making, quotations etc , Issue of Contract note

Settlement Classification of scrips (Group A, Group B, Permitted Securities), Trading Cycle & Settlement (rolling settlement, fixed period settlement), Clearing house, Pay-in and Pay-out, Types of contracts, Types of Deliveries (Hand Delivery, Spot Delivery, Special Delivery, Delivery for Clearing), Failure to deliver, Bad Deliveries and Redressal, what constitutes bad delivery (defects in certificates and transfer deed), Defaults and Redressal Procedure, Auction procedures

Share Transfers Procedures, transfer deed, stamp duty, Book Closure, record date, Ex-Dividend / Ex-Bonus / Ex-Rights / Cum-Dividend / Cum-Bonus / Cum-Rights Objections, exchange procedures related to objection, Revalidation of Transfer Deed, blank transfers, role of transfer agent

Risks in the physical delivery settlement system, Depository (concept, book transfers, dematerialisation), Clearing Corporation

Non-Tradeable Securities Procedures for bank deposits, Post Office (NSC, NSS) Companies (PSU or Private Sector Companies fixed deposits), obtaining and completing application form, Withdrawal, Premature withdrawal, Interest Accounting, Taxation etc

SECTION V RULES AND REGULATIONS

This section deals with the rules and regulations that govern securities issuance, trading and investor protection in India. Market intermediaries dealing with clients are expected to have a thorough knowledge of these regulations. The section covers legislation like the Companies Act, MRTP Act, COPRA, SEBI Act etc. and covers SEBI's regulations and circulars regarding various segments of the market.

The Companies Act (1956) and rules (1957)

Prospectus, Disclosures, Advertising and other communication (Sections 55 to 68 and Schedule II), Allotment (Sections 69 to 75), Transfer of shares (Section 108 to 112), Requirements for listing of securities, Listing Agreement/ Listing criteria, NSE/ OTCEI/ BSE/ Regional Exchanges

Securities Contracts (Regulation) Act, 1956 and Rules, 1957

Recognition of Stock Exchanges, Recognized Exchanges to submit periodical returns to SEBI, Power of SEBI to call upon exchanges or any member for any information or explanations relating to the affairs of the stock exchange or the member in relation to the stock exchange, Power of SEBI to make or amend Exchange Rules and By-laws, Power to supersede governing board of exchanges, Power to suspend business of recognized stock exchanges (Sections 3 to 12), Contracts in securities, Contracts in notified areas illegal or void in certain circumstances, Members may not act as principals in certain circumstances, Power to prohibit contracts in certain cases (Sections 13 to 16),

Qualifications for membership of recognized stock exchanges, Books of account and other documents to be preserved by the recognized stock exchanges and by their members, No member to act as a principal, in respect of any securities with any person other than a member of a recognized stock exchange, unless he has secured the consent or authority of such person and discloses this fact in the note, memorandum or agreement of sale or purchase

Indian Contract Act, 1872

Definitions and Interpretations, proposal, promise, promisor, promisee, consideration, void agreement, contract, voidable contract, void contract, Communication, acceptance and revocation of proposals, Communication when complete. Revocation of

proposals and acceptances, Revocation how made, Acceptance must be absolute, What agreements are contracts, Who are competent to contract, Consent, Free Consent, Coercion, Undue Influence, Fraud, Misrepresentation, Breach of contract and Remedies, Principal, Agent and sub-agent,

Consumer Protection Act, 1986 (COPRA)

Extent of Coverage (applies to all goods and services unless specifically exempted by the Central Government, covers all sectors whether private, public or cooperative), Provisions of the Act are compensatory in nature, Definitions (Consumer, Goods and Services, Unfair Trade Practices), Defects and deficiency, Procedures for filing complaints, District Forum, State Commission, National Commission, Relief available to consumers (removal of defects from goods, replacement of goods, refund of the price paid, award of compensation for the loss or injury suffered)

Monopolies and Restrictive Trade Practices Act, 1969

Definitions, Section 2(e) {Goods}, Section 2 (o) {Restrictive Trade practice}, Section 2(r) -Service, Section 36 A - Unfair Trading Practices - Definition, Section 36 B - Inquiry into Unfair Trade Practices by the Commission, Section 36 D - Powers exercisable by the commission inquiring into an Unfair Trade Practice

Companies (Acceptance of Deposit) Rules, 1975 as amended

These rules regulate the deposits accepted by companies from the public Section 3(1) (a), Period of deposit, Section 3(1) (c), Rate of Interest, Section 3(1)(d), Brokerage Section 3(2), Aggregate amount of deposits in relation to net owned funds , Section 3 (A), Maintenance of Liquid Assets, Section 4, Form and Particulars of the Advertisement

RBI Guidelines for Non Banking Finance Companies - Miscellaneous Non Banking Companies (Reserve Bank of India) Directions, 1977

Registration Requirements with RBI, Capital Adequacy, Periodic Reporting to RBI Credit Rating

Securities and Exchange Board of India Act, 1992 as amended

Role and Functions - General powers, Regulating the business in stock exchanges and

any other securities market, registering and regulating the working of stock brokers sub brokers, share transfer agents, bankers to issue, trustees of trust deeds, registrars to an issue, merchant bankers, underwriters, portfolio managers, investment advisors and such other intermediaries who may be associated with the securities markets in any manner,

SEBI to regulate all intermediaries in the securities business, Penalties for failure to follow rules and regulations under the Act, Power to adjudicate, Powers of Adjudicating Officer, Appellate Procedure Securities Appellate Tribunal, High Court, Central Government

SEBI Regulations and Guidelines

SEBI Guidelines on Disclosures and Investor Protection Pricing of Primary Public Issues, New companies to issue stock to public at par, New companies promoted by existing profitable companies can freely price issues, Existing profitable companies can freely price issues

SEBI (Insider Trading) Regulations The Definition of 'Insider', 'Person deemed to be a connected person', 'Unpublished Price Sensitive Information', Responsibilities of Insider

SEBI Substantial Acquisition of Shares and Takeovers Regulations 1994 Disclosures regarding substantial acquisition of shares, Continual disclosures, Takeovers

SEBI Regulations on prohibition of fraudulent and unfair trade practices relating to securities markets Prohibition against Market Manipulation, Prohibition of misleading statements to induce sale or purchase of securities, Prohibition on unfair trade practice relating to securities, Power of the Board to order investigation, Procedure for investigation, Duty to produce records, Power of the Board to issue directions, Purpose of direction, Suspension or cancellation of registration of an intermediary holding a certificate of registration

SEBI (Stock Brokers and Sub brokers) Regulations, 1992 and SEBI (Stock Brokers and Sub brokers) Rules, 1992 No stock broker or sub broker shall buy sell or deal in securities, unless he holds a certificate granted by the board under the regulations *Stock Brokers* Conditions for grant of certificate to stock broker Procedure for stock broker certification, Eligibility Criteria, *Sub Broker* General

definition of a sub broker, Conditions for grant of certificate to sub broker, Procedure for sub broker certification, Eligibility Criteria, General Obligations and Responsibilities To maintain proper books of accounts, records etc In addition, brokers must comply with record-keeping requirements established by exchanges Brokers are subject to these requirements as a condition of being an exchange member, Books of accounts and other records shall be preserved for a minimum period of five years

Registration of dealers in securities outside the stock exchanges (SEBI Press Note dated 10/5/92)

Need to show transaction price and brokerage separately in contract notes (SEBI Circular No SE/7566, dated 6/8/92)

Regulation of transactions between clients and brokers (SEBI Press Release 18/11/93 and SEBI Circular SMD/SED/2913/93) Clients' moneys to be kept in a separate account, with 'Client' in the account title, No money to be paid into clients account other than for specific purposes, No money to be withdrawn from clients account other than for specific purposes, compulsory for all member brokers to keep separate accounts for clients' securities and to keep accounts to distinguish clients' securities from own securities

Contract notes Mandatory for a broker to issue contract note to a client within 24 hours of execution of the contract

Payment/ Delivery obligations from and to clients 20% margin requirement mandatory payment/delivery by client in full within 48 hours from the issue of contract note for cash shares and 7 days for specified shares, Payments/ delivery to be made to clients within 48 hours of stock exchange payout

Precautions to be exercised by member brokers of stock exchanges while dealing on behalf of clients (SEBI letter SMD 1/23341 dated 18/11/93)

Mandatory Precautions Client personally known or introduced by a known person, record of introduction of all clients, data on clients to be maintained (Name address, telephone number and age, employment status, nature of business and address, banker and bank account number, introducer's name and address, names of all persons on whose behalf the client is operating and in case of company details of company and relevant resolutions, bank reference), Due care to be exercised

when broker is delivering broker, (Transferor Signature should be witnessed by broker or authorized sub broker, only cheque payment should be made in the name of the shareholder), If selling client name and shareholder name on certificate are different, proper enquiries should be made and a record should be maintained, Names of clients frequently delivering shares which are received under objection, to be informed to the stock exchange Names of frequently defaulting clients to be informed to the stock exchange, Brokers should insist that clients return duplicates of contract notes duly signed, No adjustment should be made between one client account and other without express authority

Guidelines: Client to provide full particulars in writing about current/ previous dealings, opinion about clients should be taken from these other member brokers, Additional details should be insisted upon like the Income Tax PAN /GR number for clients placing large orders, Caution should be exercised while executing large orders for new clients, Caution should be exercised when the clients are dealing with more than one broker, If a client habitually delays payment the broker should insist on advance payment or larger cash margin before execution, Member-brokers should not accept cash or give cash against securities Only Account Payee Cheques should be used

SEBI Portfolio Manager Rules and Regulations, 1993 Definitions *Portfolio manager, Discretionary portfolio manager, Capital Adequacy, agreement with the client, what should the contract contain, Fees charged without guaranteeing or assuring any return, fees independent of return to client, Each client's funds to be managed in accordance to the needs of each client*

Delivery - Regulations and practices of "good delivery"

Service Tax Applicability, procedures

Capital Adequacy norms for brokers Base Minimum Capital , Additional Capital Requirements related to the volume of business, Forms in which capital required to be maintained, Reporting requirement

Self-regulatory organizations (SROs) The concept of self regulation is based on the belief that the protection of public interest is in the interest of the industry Members of the industry set standards for the conduct of their business with the objective of enhancing their professionalism and their stature in the eyes of the public The Self Regulatory Organization then develops mechanisms for

enforcement of these standards on its members. The rules, regulations, ethical standards and norms are created and enforced by industry professionals knowledgeable about the business and therefore are likely to be widely accepted in the industry.

Functions of SROs Establish criteria for membership, Set ethical rules, Set rules for marketplace, Establish facilities for the punishment of violations of industry rules and regulations, Training and Continuing Education of members

Enforcement Procedures for rule violations (By laws of the BSE, NSE etc), termination of Membership, Defaulters Committee and procedure during default

SECTION VI INVESTOR PROTECTION

Investors have a right to demand disclosure of adequate information on investment products and satisfactory service from both the issuer and the intermediary selling the financial product. Several statutory and non statutory investor protection measures are in place for the benefit of investor. Statutory measures involve approaching the appropriate regulator. The most important regulators that investors should be aware are Ministry of Finance, the SEBI, the Department of Company Affairs, the Company Law Board, the Stock Exchange, the Monopolies & Restrictive Trade Practices Commission and the Consumer forums. In addition, the non statutory avenues for investor protection are available through the professional associations - the ICAI, ICWAI, ICSI, AMBI, AMFI, the brokers associations etc.

This section introduces an illustrative list of a few common investor grievances and possible remedies. While the ultimate remedy in approaching the competent civil or criminal courts is always available, the investor might save time and money from the intermediation of other forums. The reader is advised to be familiar with the sections, rules, regulations that appear in the following paragraphs.

Misleading Advertisements DCA Circular 5 (13)-CL-VI/62 dated 21/5/62, MOF No F No 1/28/SE/86 dated June 24, 1987, SEBI Clarification No IX dated 11th October 1993, RBI Non-Banking Financial Companies and Miscellaneous Non-Banking Companies (Advertisement) Rules, 1977, Section 68 & 621 of the Companies Act, 1956, Section 36 (A) of MRTP Act, Section 9 of COPRA and Stock Exchanges with reference to MoF letter Nos F 1/1/SE/74 dated 9/10/75, F 14/3/SE/76 dated 12/3/76 and No F 1/23/SE/86 dated 22nd May 1986

Disclosures in Prospectus The investors right to true and adequate disclosures is reinforced by several regulatory authorities Schedule II under Section 56 & Section 62 of the Companies Act 1956, SEBI guidelines for Disclosure and Investor Protection, RMB(DIP Series) circular No 1 (1993-94) dated April 7, 1993 and SEBI clarifications I to IX

Delay in Listing of Securities Section 73 & 621 of the Companies Act 1956, Rule 19 of Securities Contracts (Regulation) Rules 1957, Complaint to DCA, SEBI & MOF

Delay in Despatch of Securities Under Section 53, 113, 621 of Companies Act 1956, Ccomplain to DCA, CLB, SEBI & MOF

Delay in Transfer of Securities Section 53, 111 of the Companies Act 1956, Section 22(A) of the SCAR, 1956, Section 9, 11, 17 and 21 of COPRA

Trading in Odd Lots MoF circular No F 14/7/SE/85 dated 14th April 1986, Even the financial institutions like GIC, Canara Bank, UTI and few companies introduce schemes which provide added liquidity to odd lot trading

Stock Market Transactions The complaints could relate to non-receipt of securities even after payments, excess brokerage, short or delayed payments, non-furnishing of contract notes, shares switching, duplicate shares etc Arbitration Procedures of stock exchanges allow for recovery of monetary losses Hearing & Appeals Member- Non member Arbitration (Decision may be appealed to courts) and the Investor Protection Fund at the stock exchanges File a civil suit or file a criminal complaint under the Indian Penal Code and complain to SEBI

Default in Re-Payment of Deposits Section 58(A) of the Companies Act and the Companies (Acceptance of Deposits) Rules, 1975, Companies under the BIFR, Relief Undertakings, Section 12 of COPRA

Delay in Payment of Interest on Debentures Copy of the Trust Deed from the company under Section 118 of the Companies Act, 1956, Meeting of debenture holders and Section 12 of COPRA

Non-Payment of Dividends Section 205A, 207 and 621 of the Companies Act, 1956 and Section 12 of COPRA

Insider Trading and Unfair Trade Practices SEBI (Insider Trading) Regulations

1992 & Cheating under Indian Penal Code

Complaints Against Commercial Banks Investors having complaints against commercial banks can approach the local customer service committees. They can also approach the regional zonal and head office of that bank. In addition, they can approach the regional offices or central office of the RBI. Recently they have an option to approach the bank ombudsmen for any specific corruption complaints against the bank staff. The reading list may have to be prescribed in consultation with the RBI who have issued several circulars on the issue. The most important one is DBOD No ROC GC 22/C 408C(P)-83 dated April 22, 1983.

Non banking Financial Companies The NBFCs include the hire purchase finance companies, equipment leasing companies, housing companies and other loan companies. These are primarily regulated by the Reserve Bank of India under Non Banking Financial Companies Directions.

Code of Conduct Violations All professionals advising on and selling investment products are subject to code of conduct. A few intermediaries like merchant bankers, brokers, sub brokers, registrars, bankers to an issue, debenture trustees, mutual funds, FIIs are subject to statutory codes of conduct prescribed by SEBI. Other professionals like chartered accountants, company secretaries, cost and work accountants have their code of conduct enforced by the respective SRO. Most of these codes prescribe satisfactory service, truthful disclosure of conflicts and fair market practices for their members. Investors hurt by the intermediaries or professional conduct could complain to the respective statutory body or the SRO. Section VII enumerates the codes of conduct prescribed for different class of professionals.

SECTION VII ETHICS AND CODES OF CONDUCT

Intermediaries in the market are expected to adhere to and maintain a high standard of fairness and integrity in their dealings with other market participants and their clients. Market intermediaries should exercise due diligence, disclose any conflicts, maintain confidentiality, and provide the best advice to clients. Compliance with statutory requirements, adherence to trading practices, having capabilities to service customers etc. are mandated by the industry's codes of conduct. Adherence to these codes of conduct is essential to build a higher level of investor confidence in the Indian securities markets.

*Code of Conduct under SEBI (Merchant Bankers) Regulations, 1992,
Code of Conduct under SEBI (Underwriters) Regulations, 1993,
Code of Conduct under SEBI (Registrars to an Issue and Share Transfer Agents)
Regulations, 1993,
Code of Conduct for Brokers (Regulation 7) and Code of Conduct for Sub-brokers
(Regulation 15) under Securities and Exchange Board of India (Stock Brokers and
Sub-brokers) Regulations 1992,
Code of Ethics for Agents and Representatives of Unit Trust of India*

*Self-regulatory organizations (SROs) like stock exchanges, professional associations
etc have codes of conducts for their members*

*Code of Conduct for NSE trading members
Code of Conduct for OTCEI members and dealers*

*BSE By laws also define misconduct, unbusinesslike conduct and unprofessional
conduct*

*Misconduct (Section 356), Unbusinesslike conduct (Section 357), Unprofessional
conduct (Section 358)*

*Codes of Conduct of Professional Associations like the Institute of Chartered
Accountants of India, Institute of Cost and Works Accountants of India, Institute of
Company Secretaries of India etc are applicable for the members of these
associations*

*Professional Misconduct is defined in the First and Second Schedule of the
Chartered Accountants Act, 1949, Cost and Works Accountants Act, 1959 and
Company Secretaries Act , 1980*

Current Developments:

*The readers are advised to refer to current developments in the above subject area
from time to time The reader is also advised to refer to latest guidelines, regulations,
procedures, products etc related to the above areas*