MARKET BASIC

1. What are the various types of financial markets?

The financial markets can broadly be divided into money and capital market.

Money Market: Money market is a market for debt securities that pay off in the short term usually less than one year, for example the market for 90-days treasury bills. This market encompasses the trading and issuance of short term non equity debt instruments including treasury bills, commercial papers, bankers acceptance, certificates of deposits, etc.

Capital Market: Capital market is a market for long-term debt and equity shares. In this market, the capital funds comprising of both equity and debt are issued and traded. This also includes private placement sources of debt and equity as well as organized markets like stock exchanges. Capital market can be further divided into primary and secondary markets.

2. What is meant by the Secondary Market?

Secondary Market refers to a market where securities are traded after being initially offered to the public in the primary market and/or listed on the Stock Exchange. Majority of the trading is done in the secondary market. Secondary market comprises of equity markets and the debt markets.

For the general investor, the secondary market provides an efficient platform for trading of his securities. For the management of the company, Secondary equity markets serve as a monitoring and control conduit—by facilitating value-enhancing control activities, enabling implementation of incentive-based management contracts, and aggregating information (via price discovery) that guides management decisions.

3. What is the difference between the primary market and the secondary market?

In the primary market, securities are offered to public for subscription for the purpose of raising capital or fund. Secondary market is an equity trading avenue in which already existing/pre- issued securities are traded amongst investors. Secondary market could be either auction or dealer market. While stock exchange is the part of an auction market, Over-the-Counter (OTC) is a part of the dealer market.

4. What is SEBI and what is its role?

The SEBI is the regulatory authority established under Section 3 of SEBI Act 1992 to protect the interests of the investors in securities and to promote the development of, and to regulate, the securities market and for matters connected therewith and incidental thereto.

5. What are the products dealt in the secondary markets?

Following are the main financial products/instruments dealt in the secondary market:

Equity: The ownership interest in a company of holders of its common and preferred stock. The various kinds of equity shares are as follows –

- Rights Issue/ Rights Shares: The issue of new securities to existing shareholders at a ratio to those already held.
- Bonus Shares: Shares issued by the companies to their shareholders free of cost by capitalization of accumulated reserves from the profits earned in the earlier years.
- Preferred Stock/ Preference shares: Owners of these kind of shares are entitled to a fixed dividend or dividend calculated at a fixed rate to be paid regularly before dividend can be paid in respect of equity share. They also enjoy priority over the equity shareholders in payment of surplus. But in the event of liquidation, their claims rank below the claims of the company's creditors, bondholders / debenture holders.
- Cumulative Preference Shares. A type of preference shares on which dividend accumulates if remains unpaid. All arrears of preference dividend have to be paid out before paying dividend on equity shares.
- Cumulative Convertible Preference Shares: A type of preference shares where the dividend payable on the same accumulates, if not paid. After a specified date, these shares will be converted into equity capital of the company.
- Participating Preference Share: The right of certain preference shareholders to participate in profits after a specified fixed dividend contracted for is paid. Participation right is linked with the quantum of dividend paid on the equity shares over and above a particular specified level.
- Security Receipts: Security receipt means a receipt or other security, issued by a securitisation company or reconstruction company to any qualified institutional buyer pursuant to a scheme, evidencing the purchase or acquisition by the holder thereof, of an undivided right, title or interest in the financial asset involved in securitisation.
- Government securities (G-Secs): These are sovereign (credit risk-free) coupon bearing instruments which are issued by the Reserve Bank of India on behalf of Government of India, in lieu of the Central Government's market borrowing programme. These securities have a fixed coupon that is paid on specific dates on half-yearly basis. These securities are available in wide range of maturity dates, from short dated (less than one year) to long dated (upto twenty years).

Debentures: Bonds issued by a company bearing a fixed rate of interest usually payable half yearly on specific dates and principal amount repayable on particular date on redemption of the debentures. Debentures are normally secured/ charged against the asset of the company in favour of debenture holder.

Bond: A negotiable certificate evidencing indebtedness. It is normally unsecured. A debt security is generally issued by a company, municipality or government agency. A bond investor lends money to the issuer and in exchange, the issuer promises to repay the loan amount on a specified maturity date. The issuer usually pays the bond holder periodic interest payments over the life of the loan. The various types of Bonds are as follows-

- Zero Coupon Bond: Bond issued at a discount and repaid at a face value. No periodic interest is paid. The difference between the issue price and redemption price represents the return to the holder. The buyer of these bonds receives only one payment, at the maturity of the bond.

- Convertible Bond: A bond giving the investor the option to convert the bond into equity at a fixed conversion price.

Commercial Paper: A short term promise to repay a fixed amount that is placed on the market either directly or through a specialized intermediary. It is usually issued by companies with a high credit standing in the form of a promissory note redeemable at par to the holder on maturity and therefore, doesn't require any guarantee. Commercial paper is a money market instrument issued normally for a tenure of 90 days.

Treasury Bills: Short-term (up to 91 days) bearer discount security issued by the Government as a means of financing its cash requirements.

6. Whom should I contact for my Stock Market related transactions?

You can contact a broker or a sub broker registered with SEBI for carrying out your transactions pertaining to the capital market.

7. Who is a broker?

A broker is a member of a recognized stock exchange, who is permitted to do trades on the screen-based trading system of different stock exchanges. He is enrolled as a member with the concerned exchange and is registered with SEBI.

8. Who is a sub broker?

A sub broker is a person who is registered with SEBI as such and is affiliated to a member of a recognized stock exchange.

9. How do I know if the broker or sub broker is registered?

You can confirm it by verifying the registration certificate issued by SEBI. A broker's registration number begins with the letters "INB" and that of a sub broker with the letters "INS". For the brokers of derivatives segment, the registration number begins with the letters "INF". There is no sub-broker in the derivatives segment.

10. Am I required to sign any agreement with the broker or sub-broker?

Yes. For the purpose of engaging a broker to execute trades on your behalf from time to time and furnish details relating to yourself for enabling the broker to maintain client registration form you have to sign the "Member - Client agreement" if you are dealing directly with a broker. In case you are dealing through a sub-broker then you have to sign a "Broker - Sub broker - Client Tripartite Agreement". The Model Agreement between Broker-Client / Broker -Sub Broker - Client and Know your Client Form can be viewed from SEBI Website at www.sebi.gov.in. Model Tripartite Agreement between Broker-Sub broker and Clients is applicable only for the cash segment. The Model Agreement has to be executed on the non-judicial stamp paper. The Agreement contains clauses defining the rights and responsibility of Client vis-à-vis broker/ sub broker. The documents prescribed are model formats. The stock exchanges/stock broker may incorporate any additional clauses in these documents provided these are not in conflict with any of the clauses in the model document, as also the Rules, Regulations, Articles, Byelaws, circulars, directives and guidelines.

11. What is Member –Client Agreement Form?

This form is an agreement entered between client and broker in the presence of witness where the client agrees (is desirous) to trade/invest in the securities listed on the concerned Exchange through the broker after being satisfied of brokers capabilities to deal in securities. The member, on the other hand agrees to be satisfied by the genuineness and financial soundness of the client and making client aware of his (broker's) liability for the business to be conducted.

12. What kind of details do I have to provide in Client Registration form?

This form is an agreement entered between client and broker in the presence of witness where the client agrees (is desirous) to trade/invest in the securities listed on the concerned Exchange through the broker after being satisfied of brokers capabilities to deal in securities. The member, on the other hand agrees to be satisfied by the genuineness and financial soundness of the client and making client aware of his (broker's) liability for the business to be conducted.

- Your name, date of birth, photograph, address, educational qualifications, occupation, residential status(Resident Indian/ NRI/others)
- Unique Identification Number (wherever applicable)
- Bank and depository account details
- Income tax No. (PAN/GIR) which also serves as unique client code.
- If you are registered with any other broker, then the name of broker and concerned Stock exchange and Client Code Number.
- Proof of identity submitted either as MAPIN UID Card/Pan No./Passport/Voter ID/Driving license/Photo Identity card issued by Employer registered under MAPIN

For proof of address (any one of the following):

- Passport
- Voter ID
- Driving license
- Bank Passbook
- Rent Agreement
- Ration Card
- Flat Maintenance Bill
- Telephone Bill
- Telephone Bill
- Electricity Bill
- Certificate issued by employer registered under MAPIN
- Insurance Policy

Each client has to use one registration form. In case of joint names /family members, a separate form has to be submitted for each person.

In case of Corporate Client, following information has to be provided:

- Name, address of the Company/Firm
- Unique Identification Number (wherever applicable)
- Date of incorporation and date of commencement of business.
- Registration number(with ROC, SEBI or any government authority)
- Details of PAN Account Number:
- Details of Promoters/Partners/Key managerial Personnel of the Company/Firm in specified format.
- Bank and Depository Account Details
- Copies of the balance sheet for the last 2 financial years (copies of annual balance sheet to be submitted every year)
- Copy of latest share holding pattern including list of all those holding more than 5% in the share capital of the company, duly certified by the Company Secretary / Whole time Director/MD. (copy of updated shareholding pattern to be submitted every year)
- Copies of the Memorandum and Articles of Association in case of a company / body incorporate / partnership deed in case of a partnership firm
- Copy of the Resolution of board of directors' approving participation in equity / derivatives / debt trading and naming authorized persons for dealing in securities.
- Photographs of Partners/Whole time directors, individual promoters holding 5% or more, either directly or indirectly, in the shareholding of the company and of persons authorized to deal in securities.
- If registered with any other broker, then the name of broker and concerned Stock exchange and Client Code Number.

13. What is meant by Unique Client Code?

In order to facilitate maintaining database of their clients, it is mandatory for all brokers to use unique client code which will act as an exclusive identification for the client. For this purpose, PAN number/passport number/driving License/voters ID number/ ration card number coupled with the frequently used bank account number and the depository beneficiary account can be used for identification, in the given order, based on availability.

14. What is a risk disclosure document?

In order to acquaint the investors in the markets of the various risks involved in trading in the stock market, the members of the exchange have been required to sign a risk disclosure document with their clients, informing them of the various risks like risk of volatility, risks of lower liquidity, risks of higher spreads, risks of new announcements, risks of rumours etc.

15. How do I place my orders with the broker or sub broker?

You can either go to the broker's /sub broker's office or place an order over the phone /internet or as defined in the Model Agreement given above.

16. How do I know whether my order is placed?

The Stock Exchanges assign a Unique Order Code Number to each transaction, which is intimated by broker to his client and once the order is executed, this order code number is printed on the contract note. The broker member has also to maintain the record of time when the client has placed order and reflect the same in the contract note along with the time of execution of the order.

17. What documents should be obtained from broker on execution of trade?

You have to ensure receipt of the following documents for any trade executed on the Exchange:

- a. Contract note in Form A to be given within stipulated time.
- b. In the case of electronic issuance of contract notes by the brokers, the clients shall ensure that the same is digitally signed and in case of inability to view the same, shall communicate the same to the broker, upon which the broker shall ensure that the physical contract note reaches the client within the stipulated time

It is the contract note that gives rise to contractual rights and obligations of parties of the trade. Hence, you should insist on contract note from stock broker.

18. What is the maximum brokerage that a broker/sub broker can charge?

The maximum brokerage that can be charged by a broker has been specified in the Stock Exchange Regulations and hence, it may differ from across various exchanges. As per the BSE & NSE Bye Laws, a broker cannot charge more than 2.5% brokerage from his clients. This maximum brokerage is inclusive of the brokerage charged by the sub-broker. Further, SEBI (Stock brokers and Sub brokers) Regulations, 1992 stipulates that sub broker cannot charge from his clients, a commission which is more than 1.5% of the value mentioned in the respective purchase or sale note.

19. What are the charges that can be levied on the investor by a stock broker/sub broker?

The trading member can charge:

- 1. Brokerage charged by member broker.
- 2. Penalties arising on specific default on behalf of client (investor)
- 3. Service tax as stipulated.
- 4. Securities Transaction Tax (STT) as applicable.
- 5. Stamp Duty, as per the rate of respective state
- 6. Transaction charge

20. What is STT?

Securities Transaction Tax (STT) is a tax being levied on all transactions done on the stock exchanges at rates prescribed by the Central Government from time to time. Pursuant to the enactment of the Finance (No.2) Act, 2004, the Government of India notified the Securities Transaction Tax Rules, 2004 and STT came into effect from October 1, 2004.

21. What is an Account Period Settlement?

An account period settlement is a settlement where the trades pertaining to a period stretching over more than one day are settled. For example, trades for the period Monday to Friday are settled together. The obligations for the account period are settled on a net basis. Account period settlement has been discontinued since January 1, 2002, pursuant to SEBI directives.

22. What is a Rolling Settlement?

In a Rolling Settlement trades executed during the day are settled based on the net obligations for the day.
Presently the trades pertaining to the rolling settlement are settled on a T+2 day basis where T stands for the trade day. Hence, trades executed on a Monday are typically settled on the following Wednesday (considering 2 working days from the trade day). The funds and securities pay-in and pay-out are carried out on T+2 day.

23. What is the pay-in day and pay- out day?

Pay in day is the day when the brokers shall make payment or delivery of securities to the exchange. Pay out day is the day when the exchange makes payment or delivery of securities to the broker. Settlement cycle is on T+2 rolling settlement basis w.e.f. April 01, 2003. The exchanges have to ensure that the pay out of funds and securities to the clients is done by the broker within 24 hours of the payout. The Exchanges will have to issue press release immediately after pay out.

24. What are the prescribed pay-in and pay-out days for funds and securities for Normal Settlement?

The pay-in and pay-out days for funds and securities are prescribed as per the Settlement Cycle. A typical Settlement Cycle of Normal Settlement is given below:

	Activity	Day
Trading	Rolling Settlement Trading	T
Clearing	Custodial Confirmation	T+1 working days
	Delivery Generation	T+1 working days
Settlement	Securities and Funds pay in	T+2 working days
	Securities and Funds pay out	T+2 working days
Post Settlement	Valuation Debit	T+2 working days
	Auction	T+3 working days
	Bad Delivery Reporting	T+4 working days
	Auction settlement	T+5 working days

	Close out	T+5 working days
	Rectified bad delivery pay-in and pay-out	T+6 working days
	Re-bad delivery reporting and pickup	T+8 working days
	Close out of re-bad delivery	T+9 working days

Note: The above is a typical settlement cycle for normal (regular) market segment. The days prescribed for the above activities may change in case of factors like holidays, bank closing etc. You may refer to scheduled dates of pay-in/pay-out notified by the Exchange for each settlement from time-to-time.

25. In case of purchase of shares, when do I make payment to the broker?

The payment for the shares purchased is required to be done prior to the pay in date for the relevant settlement or as otherwise provided in the Rules and Regulations of the Exchange.

26. In case of sale of shares, when should the shares be given to the broker?

The delivery of shares has to be done prior to the pay in date for the relevant settlement or as otherwise provided in the Rules and Regulations of the Exchange and agreed with the broker/sub broker in writing.

27. How long it takes to receive my money for a sale transaction and my shares for a buy transaction?

Brokers were required to make payment or give delivery within two working days of the pay - out day. However, as settlement cycle has been reduced fromT+3 rolling settlement to T+2 w.e.f. April 01, 2003, the pay out of funds and securities to the clients by the broker will be within 24 hours of the payout.

28. Is there any provision where I can get faster delivery of shares in my account?

The investors/clients can get direct delivery of shares in their beneficiary accounts. To avail this facility, you have to give details of your beneficiary account and the DP-ID of your DP to your broker along with the Standing Instructions for 'Delivery-In' to your Depository Participant for accepting shares in your beneficiary account. Given these details, the Clearing Corporation/Clearing House shall send pay out instructions to the depositories so that you receive pay out of securities directly into your beneficiary account.

29. What is an Auction?

The Exchange purchases the requisite quantity in the Auction Market and gives them to the buying trading member. The shortages are met through auction process and the difference in price indicated in contract note and price received through auction is paid by member to the Exchange, which is then liable to be recovered from the client.

30. What happens if the shares are not bought in the auction?

If the shares could not be bought in the auction i.e. if shares are not offered for sale in the auction, the transactions are closed out as per SEBI guidelines. The guidelines stipulate that "the close out Price will be the highest price recorded in

that scrip on the exchange in the settlement in which the concerned contract was entered into and upto the date of auction/close out OR 20% above the official closing price on the exchange on the day on which auction offers are called for (and in the event of there being no such closing price on that day, then the official closing price on the immediately preceding trading day on which there was an official closing price), whichever is higher.
Since in the rolling settlement the auction and the close out takes place during trading hours, the reference price in the rolling settlement for close out procedures would be taken as the previous day's closing price.

31. What recourses are available to me for redressing my grievances?

If the shares could not be bought in the auction i.e. if shares are not offered for sale in the auction, the transactions are closed out as per SEBI guidelines.
Office of Investor Assistance and Education (OIAE) : You can lodge a complaint with OIAE Department of SEBI against companies for delay, non-receipt of shares, refund orders, etc., and with Stock Exchanges against brokers on certain trade disputes or non receipt of payment/securities.
Arbitration: If no amicable settlement could be reached, then you can make application for reference to Arbitration under the Bye Laws of concerned Stock Exchange.
Court of Law

32. What is Arbitration?

Arbitration is an alternative dispute resolution mechanism provided by a stock exchange for resolving disputes between the trading members and their clients in respect of trades done on the exchange.

33. What is the process for preferring arbitration?

The byelaws of the exchange provide the procedure for Arbitration. You can procure a form for filing arbitration from the concerned stock exchange. The arbitral tribunal has to make the arbitral award within 3 months from the date of entering upon the reference. The time taken to make an award cannot be extended beyond a maximum period of 6 months from the date of entering upon the reference.

34. Who appoints the arbitrators?

Every exchange maintains a panel of arbitrators. Investors may choose the arbitrator of their choice from the panel. The broker also has an option to choose an arbitrator. The name(s) would be forwarded to the member for acceptance. In case of disagreement, the exchange shall decide upon the name of arbitrators.

35. What happens if I am aggrieved by the award of the arbitrator?

In case you are aggrieved by the arbitration award, you can take recourse to the appeal provisions as given in the bye-laws of the Exchange.

36. What is Investor Protection Fund (IPF)/ Customer Protection Fund (CPF) at Stock Exchanges?

Investor Protection Fund is the fund set up by the Stock Exchanges to meet the legitimate investment claims of the clients of the defaulting members that are not of speculative nature. SEBI has prescribed guidelines for utilisation of IPF at the Stock Exchanges. The Stock Exchanges have been permitted to fix suitable compensation limits, in consultation with the IPF/CPF Trust. It has been provided that the amount of compensation available against a single claim of an investor arising out of default by a member broker of a Stock Exchange shall not be less than Rs. 1 lakh in case of major Stock Exchanges viz., BSE and NSE, and Rs. 50,000/- in case of other Stock Exchanges.

37. What is the traditional structure of the stock exchanges in India?

There are 22 recognised stock exchanges in India. Mangalore Stock Exchange was refused renewal of recognition vide SEBI order dated August 31, 2004. In terms of legal structure, the stock exchanges in India could be segregated into two broad groups – 19 stock exchanges which were set up as companies, either limited by guarantees or by shares, and the 3 stock exchanges which were associations of persons (AOP) viz. BSE, ASE and Madhya Pradesh Stock Exchange. The 19 stock exchanges which have been functioning as companies include: the stock exchanges of Bangalore, Bhubaneswar, Calcutta, Cochin, Coimbatore, Delhi, Gauhati, Hyderabad, Interconnected SE, Jaipur, Ludhiana, Madras, Magadh, NSE, Pune, OTCEI, Saurashtra-Kutch, Uttar Pradesh, and Vadodara. Apart from NSE, all stock exchanges whether established as corporate bodies or Association of Persons (AOPs), were non-profit making organizations.

38. What is meant by corporatisation of stock exchanges?

Corporatisation is the process of converting the organizational structure of the stock exchange from a non-corporate structure to a corporate structure. Traditionally, some of the stock exchanges in India were established as “Association of persons”, e.g. the Stock Exchange, Mumbai (BSE), Ahmedabad Stock Exchange (ASE) and Madhya Pradesh Stock Exchange (MPSE). Corporatisation of such exchanges is the process of converting them into incorporated Companies.

39. What is demutualisation of stock exchanges?

Demutualisation refers to the transition process of an exchange from a “mutually-owned” association to a company “owned by shareholders”. In other words, transforming the legal structure of an exchange from a mutual form to a business corporation form is referred to as demutualisation. The above, in effect means that after demutualisation, the ownership, the management and the trading rights at the exchange are segregated from one another.

40. How is a demutualised exchange different from a mutual exchange?

In a mutual exchange, the three functions of ownership, management and trading are intervened into a single Group. Here, the broker members of the exchange are both the owners and the traders on the exchange and they further manage the exchange as well. A demutualised exchange, on the other hand, has all these three functions clearly segregated, i.e. the ownership, management and trading are in separate hands.

41. Currently are there any demutualised stock exchanges in India?

Currently, two stock exchanges in India, the National Stock Exchange (NSE) and Over the Counter Exchange of India (OTCEI) are not only corporatised but also demutualised with segregation of ownership and trading rights of members. The Corporatisation and Demutualisation Schemes of 19 stock exchanges (other than NSE, OTCEI, Mangalore Stock Exchange and Coimbatore Stock exchange) have been notified by SEBI and are at various stages of implementation.