Dematerialization

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Abstract- *This paper is attempted to know the level of understanding on dematerialization of shares among the retail investors in India. In the process, the theoretical aspects of dematerialization like need and importance, benefits, and procedure for it are presented as a prelude to the empirical analysis. It is found from the study that all the sample investors had a demat account except very little amount. Majority of the investors had all their shares in demat form. Still there is a need to create awareness among retail investors and encourage them to dematerialize their shares that have not done. 'Not understanding the dematerialization system and account maintenance charges' are the major reasons cited for partial dematerialization of shares.*

Keywords- Retail, Investors, Equity Shares, Dematerialization

I. INTRODUCTION

Dematerialisation is the process of converting the physical form of shares into electronic form. Prior to dematerialisation the Indian stock markets have faced several problems like delay in the transfer of certificates, forgery of certificates etc. Dematerialisation helps to overcome these problems as well as reduces the transaction time as compared to the physical segment.

According to the Depositories Act, 1996, an investor has the option to hold shares either in physical or electronic form .The process of converting the physical form of shares into electronic form is called dematerialisation or in short demats. The converted electronic data is stored with the depository from where they can be traded. It is similar to a bank where an investor opens an account with any of the depository participants. Depository participant is a representative of the depository .The DP maintains the investors securities account balances and intimates him about the status of holdings.

Dematerialisation offers flexibility along with security and convenience. Holding share certificates in physical format carried risks like certificate forgeries, loss of important share certificates, and consequent delays in certificate transfers. Dematerialization eliminates these hassles by allowing customers to convert their physical certificates into electronic format.

Background

Indian capital market has seen unprecedented boom in its activity in the last 15 years in terms of number of stock exchanges, listed companies, trade volumes, market intermediaries, investor population, etc. However, this surge in activity has brought with it numerous problems that threaten the very survival of the capital markets in the long run, most of which are due to the large volume of paper work involved and paper based trading, clearing and settlement.

Until the late eighties, the common man kept away from capital market and thus the quantum of funds mobilized through the market was meager. A major problem, however, continued to plague the market. The Indian markets were drowned in shares in the form of paper and hence it was problematic to handle them. Fake and stolen shares, fake signatures and signature mismatch, duplication and mutilation of shares, transfer problems, etc. The investors were scared and were under compensated for the risk borne by them. The century old system of trading and settlement requires handling of huge volumes of paper work. This has made the investors, both retail and institutional, wary of entering the capital market. However, lack of modernization become a hindrance to growth and resulted in creation of cumbersome procedures and paper work.

However, the real growth and change occurred from mid-eighties in the wake of liberalization initiatives of the Government. The reforms in the financial sector were envisaged in the banking sector, capital market, securities market regulation, mutual funds, foreign investments and Government control. These institutions and stock exchanges experienced that the certificates are the main cause of investors` disputes and arbitration cases. Since the paper work was not matching the rapid growth so there was a need for a better system to ensure removal of these impediments. Government of India decided to set up a fully automated and high technology based model exchange that could offer screen-based trading and depositories as the ultimate answer to all such reforms and eliminate various bottlenecks in the capital market, particularly, the clearing and settlement system in stock exchanges. A depository invery simple terms is a pool of pre-verified shares held in electronic mode which offers settlement of transactions in an efficient and effective way.

Process of dematerialization

- Dematerialization starts with opening a Demat account. For Demat account opening,you need to shortlist a Depository Participant (DP) that offers Demat services.
- To convert the physical shares into electronic/Demat form, A Dematerialization Request Form (DRF), which is available with the Depository Participant (DP), has to be filled in and deposited along with share certificates. On each share certificate, *'Surrendered for Dematerialization'* needs to be mentioned.
- The DP needs to process this request along with the share certificates to the company and simultaneously to registrars and transfer agents through the depository.
- Once the request is approved, the share certificates in the physical form will be destroyed and a confirmation of dematerialization will be sent to the depository.
- The depository will then confirm the dematerialization of shares to the DP. Once this is done, a credit in the holding of shares will reflect in the investor's account electronically.
- This cycle takes about 15 to 30 days from the submission of dematerialization request.
- Dematerialization is possible only with a Demat account, therefore it is essential to learn how to open a Demat account to understand dematerialization.

Purchasing Dematerialised securities:

Step 1: Choose a broker who can facilitate the purchase of the securities.
Step 2: Make a payment to the broker who will then arrange for the payment to the clearing corporation on the pay-in day.
Step 3: The securities are credited to the broker's clearing account on the pay-out day.
Step 4: The broker will give instructions to its Depository Participant (DP) to debit the clearing account and credit the same to your account.
Step 5: The depository will then confirm the dematerialization of shares to the DP. Once this is done, a credit in the holding of shares will reflect in the investor's account electronically.
Step 6: You will receive shares into your account. In order to receive the credit, you will need to give 'Receipt Instructions to the DP if you did not give standing instructions during the opening of your account.

Selling Dematerialized securities:

Step 1: Choose a broker and sell the securities in a stock exchange linked to the NSDL (National Securities Depository Limited)
Step 2: The Depository Participant (DP) needs to be instructed to debit your account with the number of securities sold and credit the broker's clearing account.
Step 3: You need to send the delivery instruction to your Depository Participant (DP) using the delivery instruction slips.
Step 4: Once the request is approved, the share certificates in the physical form will be destroyed and a confirmation of dematerialization will be sent to the depository.
Step 5: The broker will give instructions to its DP for delivery to the clearing corporation before the pay-in day.
Step 6: You will receive the payment from the broker for the sale of your securities.

Benefits of dematerialization

There is a wide range of benefits of dematerialisation of securities. Some of them are as follows:

1. We can conveniently manage your shares and transactions from anywhere.
2. Stamp duty is not levied on your electronic securities.
3. Holding charges levied are nominal.
4. Risks involved with physical securities such as theft, loss, forgery or damage are eliminated.
5. You can buy securities in odd lots and buy a single security.
6. Due to the elimination of paperwork, the time required for completing a transaction gets reduced.

Object Of Demat System :

India has adopted this system in which book entry is done electronically. It is the system where no paper is involved. Physical form is extinguished and shares or securities are held in electronic mode. Before the introduction of the depository system by the Depository Act, 1996, the process of sale, purchase and transfer of shares was a huge problem and the safety perspective was zero.

Demat Disadvantages :

1. The biggest limitation is that in order to have a demat account one needs to be internet savvy and therefore people who are not that literate with internet will find it hard to operate their demat account and therefore they tell their brokers or sub brokers to transact on behalf of them which sometimes lead to fraud and mismanagement of funds by the sub brokers.

2. Another limitation is that since stocks are dematerialized individuals tend to keep looking the stock price more often than they would have if stocks were in paper form and therefore they end up doing trading instead of investment, however this limitation is not of demat account but of individuals as they are not patient enough still many people blame it on demat account when they are asked why they are in a hurry to sale shares.

Need of Dematerialization

- Handling of paperwork related to shares in the physical format often led to errors and unforeseen mishaps in the past.
- Tracking records and share documents with respect to transfer and upkeep transactions was difficult.
- The authorities in charge of updating these documents could not keep up with the increasing volume of share papers, which, if left unchecked, could cripple the financial base of the Indian share market and associated businesses.

Scope of Study

- The Scope of the study is confined to the process of dematerialization of securities and its advantages.
- The Scope of the project is limited to the depository participant services through depositors.

Objectives of the Study

- To study the activities of depository participants.
- To know the advantages of dematerialization
- To study the process of settlements.
- To know the services provided by the depository participants.

Methodology of the Study

- The study is based on Secondary data only.
- The secondary data is collected from various webs.

INTRODUCTION AND NEED FOR THE STUDY

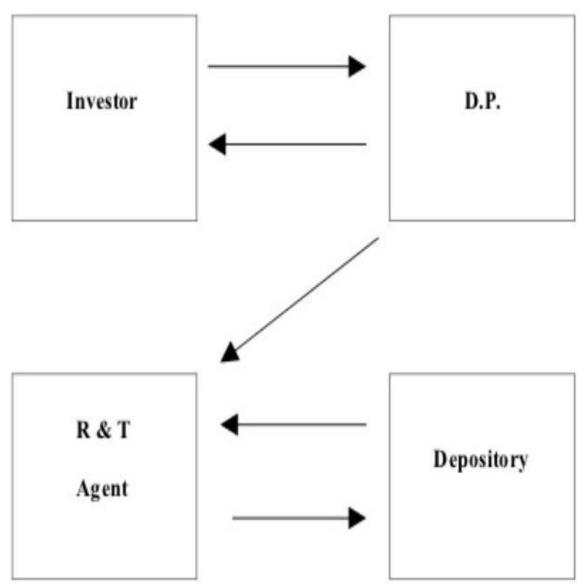
The primary market deals with the issue of new instruments by the corporate sector such as equity shares, preference shares and debt instruments. Central and state governments, various public sectors industrail units (PSUs),stautory and other authorities such as state electricity bolds and port trusts also issue based / instruments.

The primary market in which public issue of securities is made through a prospectus is a retail market and there is no physical location. The secondary market or stock exchange is a market for trading and settlement of securities that have already been issued.

The secondary market consists of 23 stock exchanges including the National stock Exchange. Over-the-Counter Exchange of India (OCTEI) and Inter Connected Stock Exchange of India Ltd. The secondary market provides a trading plan for the securities already issued to be bought and sold.

II. DATA ANALYSIS

<u>Procedure for Dematerialization</u>



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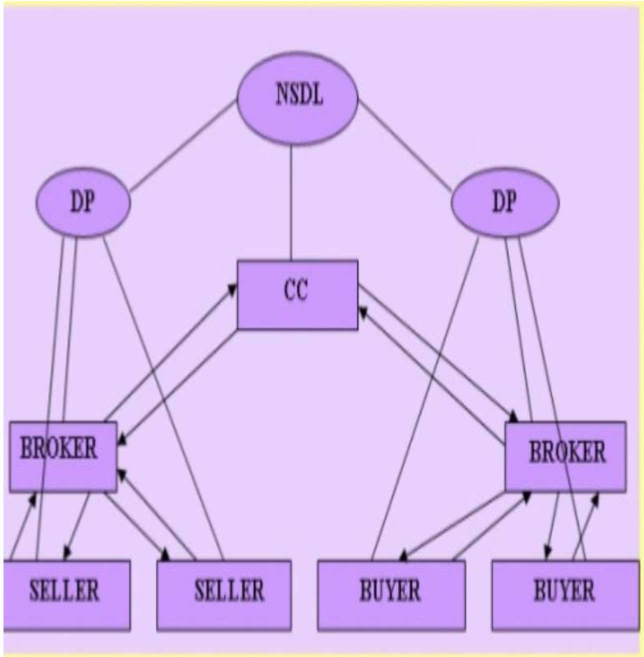

III. FINDINGS, CONCLUSION & RECOMMENDATIONS

Findings:

- Not helpful to an investor in choosing DP as charges are not comparable for different DPs.
- No benefit of multi-depositories system to the investors regarding reduction of demat charges
- Lengthy and bulky list of Headings and Sub-headings of demat retail charges
- Unjustified system to charge fees from investors on the basis offlat system as well as value based system whichever is higher.
- No maximum limit of amount of DPs charges for investors
- No transparency regarding charges charged by the NSDL and CDSL from the DPs for the investors' relevant demat operations
- Depositories have been reducing the charges for DPs from time to time but this tradition is not followed by any of the DPs.
- Pinching annual maintenance charges charged by all DPs from all investors

Conclusion:

But retail investors find it difficult to have knowledge of so many acts rather it would be too much to expect them to be aware about all the provisions, by-laws, regulations and rules available for implementation of their rights and protection against any negligence or fraud committed by the DPs.

'Investors' Charter of Rights- for demat account holders' will be helpful in safeguarding demat accountholders against negligence and frauds committed by the DPs. Specimen Charter of Rights prescribed in the present study can be utilized as base for framing such type of Charter for demat accountholders.

Demat is a public utility service. In addition to the above mentioned findings, suggestions and conclusions, the present study also explains the precautions to be taken by individual investors in different demat operations. Self-education, alertness, activeness and attentiveness of beneficial owners are the basic mantras under operational framework of Depository System.